	CLERK'S STAMP
COURT FILE NUMBER	1301 – 04364
COURT	COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
APPLICANTS	IN THE MATTER OF THE ***COMPANIES' CREDITORS ARRANGEMENT ACT***, R.S.C. 1985, c. C-36, AS AMENDED AND IN THE MATTER OF POSEIDON CONCEPTS CORP., POSEIDON CONCEPTS LTD., POSEIDON CONCEPTS LIMITED PARTNERSHIP AND POSEIDON CONCEPTS INC.
DOCUMENT	**BENCH BRIEF OF THE MONITOR, PRICEWATERHOUSECOOPERS INC.** **10:00 a.m. Tuesday, November 4, 2014**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	**BENNETT JONES LLP** Barristers and Solicitors 4500, 855 – 2nd Street SW Calgary, Alberta T2P 4K7 Attention: Ken Lenz, Q.C. Telephone No.: (403) 298-3317 Facsimile No.: (403) 265-7219 Client File No.: 11866.66

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I. NATURE OF THE APPLICATION

1. This Bench Brief is submitted on behalf of PricewaterhouseCoopers Inc., the Court-appointed Monitor (the "Monitor") of the debtor companies, Poseidon Concepts Corp., Poseidon Concepts Ltd., Poseidon Concepts Limited Partnership and Poseidon Concepts Inc. (collectively, "Poseidon").

2. Poseidon commenced these proceedings pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "CCAA") on April 9, 2013.

3. Pursuant to the Order granted by this Honourable Court on September 27, 2013, the Monitor has been granted enhanced powers to, among other things:

   (a) operate and carry on the business of Poseidon including, without limitation to negotiate, develop and implement a Plan or Plans on behalf of Poseidon;

   (b) take all steps and actions the Monitor considers necessary or desirable in these CCAA proceedings;

   (c) initiate, prosecute and continue the prosecution of any and all proceedings on behalf of Poseidon and to settle or compromise any such proceedings or claims; and

   (d) exercise any rights which Poseidon may have.

4. This application is being brought by the Monitor to extend the stay of proceedings to February 27, 2015.

5. When the Monitor advised the respective stakeholders of its proposed application to extend the stay of proceedings to February 27, 2015, counsel for certain Class Action Plaintiffs advised the Monitor that their clients would oppose the application.

6. The Class Action Plaintiffs have not advised the Monitor of the basis on which they intend to oppose the stay application. As a result, the limited purpose of this Bench Brief is to outline for the Court the applicable law regarding CCAA stay extension applications.

II. ISSUE

7. What factors is the Court consider when deciding whether to grant an extension of a CCAA stay of proceedings?

III. FACTS

8. The Monitor is filing, concurrently with this Brief of Argument, its Twentieth Report to the Court, in which it updates the Court and the stakeholders as to the current status of these CCAA proceedings and the progress that is expected to be achieved during the extension period being requested.

IV. LAW

A. The Relevant Provisions in the CCAA

9. The Court is given broad discretion in s. 11.02(2) of the CCAA to make a stay extension order on any terms it deems fit:

> **Stays, etc. — other than initial application**
>
> (2) A court may, on an application in respect of a debtor company other than an initial application, make an order, on any terms that it may impose,
>
> > (*a*) staying, until otherwise ordered by the court, for any period that the court considers necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in paragraph (1)(*a*);
> >
> > (*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
> >
> > (*c*) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

- CCAA, s. 11.02(2) **[TAB 1]**

10. To obtain the extension of a stay, the applicant must establish that: circumstances exist which make the order appropriate; and the applicant is acting in good faith and with due diligence:

Burden of proof on Application

11.02(3) The court shall not make the order unless

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

(*b*) in the case of an order under subsection (2), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

- CCAA, s. 11.02(3) **[TAB 1]**

B. Judicial Interpretation of the Statutory Test

1. Whether the Order to Extend the Stay is Appropriate

11. In considering whether "circumstances exist that make the order appropriate", the court must be satisfied that an extension of the stay will further the purposes of the CCAA.

- *Re Worldspan Marine Inc*, 2011 BCSC 1758 at para. 13 **[TAB 2]**

12. An extension of a stay which allows for a reasonable period of time to reorganize and propose a plan of arrangement to creditors, and prevents maneuvers for positioning among creditors in the interim, meets the basic purpose of the CCAA.

- *Rio Nevada Energy Inc.* (2000), 283 AR 146 (AB) at para. 32 **[TAB 3]**

13. The court should consider the interests of all affected constituencies in deciding whether it is appropriate to extend a stay, including secured, preferred and unsecured creditors, employees, landlords, shareholders, and the public generally. The objection of a single creditor should not prevent the extension of the stay and proceeding to attempt to work out a Plan of Arrangement under the CCAA.

- *Hunters Trailer & Marine Ltd*, 2000 ABQB 952 at para. 19 **[TAB 4]**

14. Inherent in insolvency proceedings is a balancing of interests between stakeholders. The fact that a creditor's remedies continue to be stayed and that prejudice may result to that creditor does not justify terminating the restructuring proceedings.

- *Bargain Harold's Discount Ltd v Paribas Bank of Canada*, 1992 CarswellOnt 159 at para. 35, [1992] OJ No 374 (Ont Gen Div) **[TAB 5]**

- *Rio Nevada, supra*, at para. 26 **[TAB 3]**

15. If the CCAA process is likely to yield a more favorable outcome for creditors generally than another process, such as receivership, bankruptcy or foreclosure, the extension of the stay is appropriate.

- *Caterpillar Financial Services Ltd. v. Hard-Rock Paving Co.*, 2008 CarswellOnt 4046 at paras. 5 and 7 **[TAB 6]**

- *Rio Nevada, supra*, at paras. 26 and 32 **[TAB 3]**

2. Whether the Applicant has Acted in Good Faith and with Due Diligence

16. The good faith requirement includes observance of reasonable commercial standards of fair dealings in the CCAA proceedings, the absence of intent to defraud, and a duty of honesty to the court and to the stakeholders directly affected by the CCAA process.

- *San Francisco Gifts Ltd Re*, 2005 ABQB 91 at paras. 14-17 **[TAB 7]**

17. Due diligence requires showing that the applicant is making reasonable progress in moving the restructuring forward.

- *SLMsoft Inc*, 2003 CanLii 36871 (ON SCJ) **[TAB 8]**

C. The Monitor's Support of a Stay Extension

18. The opinion of the Monitor, the Court's officer, on an application to have the stay extended carries considerable weight with the Court. Specifically, the Monitor's opinion as to whether there is a realistic possibility of a successful restructuring is a significant factor to be considered by the Court.

- *Scanwood Canada Ltd, Re*, 2011 NSSC 306 at para. 16 **[TAB 9]**

- *SLMsoft, supra*, at para. 3 **[TAB 8]**

D. The Test to be Met by a Party Seeking to Terminate the Stay

19. In *Rio Nevada*, the Court noted that the test that must be satisfied by an applicant seeking to terminate a CCAA stay of proceedings is the proceedings are "doomed to fail." The burden of proof of establishing that test rests on the applicant wishing to have the CCAA proceedings terminated. The debtor company does not have the burden, in an extension application, of proving that the proceedings are not "doomed to fail."

- *Rio Nevada , supra* at paras. 12-13 **[TAB 3]**
- *843504 Alberta Ltd Re*, 2003 ABQB 1015 at para. 5 **[TAB 10]**

20. In order to succeed on this basis and satisfy its onus, a creditor opposing the extension of the stay must show that there is no reasonable chance that any Plan would be accepted. When the final terms of the Plan of Arrangement have yet to be put forward, this requires more than a submission by the creditor that they will be unable to support any Plan of Arrangement. Such a submission must be viewed with skepticism by the Court, since commercial reality may dictate a change of position when the details of a plan of arrangement have been presented.

- *Rio Nevada, supra*, at paras. 17, 25 **[TAB 3]**
- *SLM, supra*, at para. 2 **[TAB 8]**

V. RELIEF REQUESTED

21. It is submitted that the extension of the stay of proceedings being sought is appropriate and necessary in the circumstances.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 30th day of October, 2014.

BENNETT JONES LLP

Ken Lenz, Q.C.

Estimated time for argument: 25 minutes
October 30, 2014
Calgary, Alberta

VI. LIST OF AUTHORITIES

1. *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36
2. *Re Worldspan Marine Inc*, 2011 BCSC 1758
3. *Rio Nevada Energy Inc.* (2000), 283 AR 146 (AB)
4. *Hunters Trailer & Marine Ltd*, 2000 ABQB 958
5. *Bargain Harold's Discount Ltd v Paribas Bank of Canada*, 1992 CarswellAlta 159, [1992] OJ No 374 (Ont Gen Div)
6. *Caterpillar Financial Services Ltd. v. Hard-Rock Paving Co.*, 2008 CarswellOnt 4046
7. *San Francisco Gifts Ltd Re*, 2005 ABQB 91
8. *SLMsoft Inc*, 2003 Canlii 36871 (ON SCJ)
9. *Scanwood Canada Ltd, Re*, 2011 NSSC 306
10. *843504 Alberta Ltd Re*, 2003 ABQB 1015

TAB 1

CANADA

CONSOLIDATION

CODIFICATION

Companies' Creditors Arrangement Act

Loi sur les arrangements avec les créanciers des compagnies

R.S.C., 1985, c. C-36

L.R.C. (1985), ch. C-36

Current to October 15, 2014

À jour au 15 octobre 2014

Last amended on April 1, 2013

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(3) The court may make an order prohibiting the release to the public of any cash-flow statement, or any part of a cash-flow statement, if it is satisfied that the release would unduly prejudice the debtor company and the making of the order would not unduly prejudice the company's creditors, but the court may, in the order, direct that the cash-flow statement or any part of it be made available to any person specified in the order on any terms or conditions that the court considers appropriate.

R.S., 1985, c. C-36, s. 10; 2005, c. 47, s. 127.

Interdiction de mettre l'état à la disposition du public

(3) Le tribunal peut, par ordonnance, interdire la communication au public de tout ou partie de l'état de l'évolution de l'encaisse de la compagnie débitrice s'il est convaincu que sa communication causerait un préjudice indu à celle-ci et que sa non-communication ne causerait pas de préjudice indu à ses créanciers. Il peut toutefois préciser dans l'ordonnance que tout ou partie de cet état peut être communiqué, aux conditions qu'il estime indiquées, à la personne qu'il nomme.

L.R. (1985), ch. C-36, art. 10; 2005, ch. 47, art. 127.

General power of court

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

R.S., 1985, c. C-36, s. 11; 1992, c. 27, s. 90; 1996, c. 6, s. 167; 1997, c. 12, s. 124; 2005, c. 47, s. 128.

Pouvoir général du tribunal

11. Malgré toute disposition de la *Loi sur la faillite et l'insolvabilité* ou de la *Loi sur les liquidations et les restructurations*, le tribunal peut, dans le cas de toute demande sous le régime de la présente loi à l'égard d'une compagnie débitrice, rendre, sur demande d'un intéressé, mais sous réserve des restrictions prévues par la présente loi et avec ou sans avis, toute ordonnance qu'il estime indiquée.

L.R. (1985), ch. C-36, art. 11; 1992, ch. 27, art. 90; 1996, ch. 6, art. 167; 1997, ch. 12, art. 124; 2005, ch. 47, art. 128.

Rights of suppliers

11.01 No order made under section 11 or 11.02 has the effect of

(*a*) prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided after the order is made; or

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

2005, c. 47, s. 128.

Droits des fournisseurs

11.01 L'ordonnance prévue aux articles 11 ou 11.02 ne peut avoir pour effet:

a) d'empêcher une personne d'exiger que soient effectués sans délai les paiements relatifs à la fourniture de marchandises ou de services, à l'utilisation de biens loués ou faisant l'objet d'une licence ou à la fourniture de toute autre contrepartie de valeur qui ont lieu après l'ordonnance;

b) d'exiger le versement de nouvelles avances de fonds ou de nouveaux crédits.

2005, ch. 47, art. 128.

Stays, etc. — initial application

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

(*a*) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*;

(*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

Suspension : demande initiale

11.02 (1) Dans le cas d'une demande initiale visant une compagnie débitrice, le tribunal peut, par ordonnance, aux conditions qu'il peut imposer et pour la période maximale de trente jours qu'il estime nécessaire:

a) suspendre, jusqu'à nouvel ordre, toute procédure qui est ou pourrait être intentée contre la compagnie sous le régime de la *Loi sur la faillite et l'insolvabilité* ou de la *Loi sur les liquidations et les restructurations*;

b) surseoir, jusqu'à nouvel ordre, à la continuation de toute action, poursuite ou autre procédure contre la compagnie;

(*c*) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

c) interdire, jusqu'à nouvel ordre, l'introduction de toute action, poursuite ou autre procédure contre la compagnie.

Stays, etc. — other than initial application

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

(*a*) staying, until otherwise ordered by the court, for any period that the court considers necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in paragraph (1)(*a*);

(*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(*c*) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

Suspension : demandes autres qu'initiales

(2) Dans le cas d'une demande, autre qu'une demande initiale, visant une compagnie débitrice, le tribunal peut, par ordonnance, aux conditions qu'il peut imposer et pour la période qu'il estime nécessaire :

a) suspendre, jusqu'à nouvel ordre, toute procédure qui est ou pourrait être intentée contre la compagnie sous le régime des lois mentionnées à l'alinéa (1)*a*);

b) surseoir, jusqu'à nouvel ordre, à la continuation de toute action, poursuite ou autre procédure contre la compagnie;

c) interdire, jusqu'à nouvel ordre, l'introduction de toute action, poursuite ou autre procédure contre la compagnie.

Burden of proof on application

(3) The court shall not make the order unless

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

(*b*) in the case of an order under subsection (2), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

Preuve

(3) Le tribunal ne rend l'ordonnance que si :

a) le demandeur le convainc que la mesure est opportune;

b) dans le cas de l'ordonnance visée au paragraphe (2), le demandeur le convainc en outre qu'il a agi et continue d'agir de bonne foi et avec la diligence voulue.

Restriction

(4) Orders doing anything referred to in subsection (1) or (2) may only be made under this section.

2005, c. 47, s. 128, 2007, c. 36, s. 62(F).

Restriction

(4) L'ordonnance qui prévoit l'une des mesures visées aux paragraphes (1) ou (2) ne peut être rendue qu'en vertu du présent article.

2005, ch. 47, art. 128, 2007, ch. 36, art. 62(F).

Stays — directors

11.03 (1) An order made under section 11.02 may provide that no person may commence or continue any action against a director of the company on any claim against directors that arose before the commencement of proceedings under this Act and that relates to obligations of the company if directors are under any law liable in their capacity as directors for the payment of those obligations, until a compromise or an arrangement in respect of the company, if one is filed, is sanctioned by the court or is refused by the creditors or the court.

Suspension — administrateurs

11.03 (1) L'ordonnance prévue à l'article 11.02 peut interdire l'introduction ou la continuation de toute action contre les administrateurs de la compagnie relativement aux réclamations qui sont antérieures aux procédures intentées sous le régime de la présente loi et visent des obligations de la compagnie dont ils peuvent être, ès qualités, responsables en droit, tant que la transaction ou l'arrangement, le cas échéant, n'a pas été homologué par le tribunal ou rejeté par celui-ci ou les créanciers.

Exception

(2) Subsection (1) does not apply in respect of an action against a director on a guarantee given by the director relating to the company's obligations or an action seeking injunctive relief against a director in relation to the company.

Exclusion

(2) La suspension ne s'applique toutefois pas aux actions contre les administrateurs pour les garanties qu'ils ont données relativement aux obligations de la compagnie ni aux mesures de la nature d'une injonction les visant au sujet de celle-ci.

TAB 2

2011 BCSC 1758
British Columbia Supreme Court

Worldspan Marine Inc., Re

2011 CarswellBC 3667, 2011 BCSC 1758, [2012] B.C.W.L.D. 2061, 211 A.C.W.S. (3d) 557, 86 C.B.R. (5th) 119

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

And In the Matter of the Canada Business Corporations Act, R.S.C. 1985, c. C-44 and the Business Corporations Act, S.B.C. 2002, c. 57

And In the Matter of Worldspan Marine Inc., Crescent Custom Yachts Inc., Queenship Marine Industries Ltd., 27222 Developments Ltd. and Composite FRP Products Ltd. (Petitioners)

Pearlman J.

Heard: December 16, 2011
Judgment: December 21, 2011
Docket: Vancouver S113550

Counsel: J.R. Sandrelli, J.D. Schultz for Petitioners, Worldspan Marine Inc., Crescent Custom Yachts Inc., Queenship Marine Industries Ltd., 27222 Developments Ltd. and Composite FRP Products
K. Jackson, V. Tickle for Wolrige Mahon (the "VCO"):
K.E. Siddall for Respondent, Harry Sargeant III
J. Leathley, Q.C. for Ontrack Systems Ltd.
D. Rossi for Mohammed Al-Saleh
G. Wharton, P. Mooney for Offshore Interiors Inc., Paynes Marine Group, Restaurant Design and Sales LLC, Arrow Transportation Systems and CCY Holdings Inc.
N. Beckie for Canada Revenue Agency
J. McLean, Q.C. for Comerica Bank
G. Dabbs for The Monitor

Subject: Insolvency; Corporate and Commercial

Headnote

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Initial application — Grant of stay — Extension of order

W Inc. and other debtor companies entered into agreement with S for construction of custom motor vessel — Dispute arose over cost of construction of vessel and S ceased making payments to companies under agreement — Companies ceased construction of vessel and laid off 97 employees who were working on it — Companies applied for relief under Companies' Creditors Arrangement Act (CCAA), and stay of proceedings was granted — Companies applied under s. 11.02(2) of CCAA for extension of stay — S opposed companies' application, claiming that they had shown lack of good faith by failing to disclose to Court that one of W Inc.'s principals was suing another of its principals for fraud in US District Court (US action) — Evidence filed in US action included demand letter which referred to deliberate overcharging of S under terms of agreement — Application for extension of stay granted — Companies had met onus of

establishing that extension order was appropriate, and that they had acted and were acting in good faith and with due diligence — Federal Court of Canada (FCC) had exercised its jurisdiction over vessel, and in rem claims against vessel would need to be determined before companies' creditors would be in position to vote on plan of arrangement — International yacht broker FY had expressed confidence that it would be able to find buyer for vessel during up-coming buying season — Companies were in discussions with potential debtors in possession (DIP) lenders for DIP facility that would be used to complete construction of vessel — Resumption of construction of vessel by companies would permit companies to resume operations and generate cash flow, and was best way to maximize return on vessel — Allegations against principal of W Inc. in US action were not yet proven, and did not involve dishonesty, bad faith or fraud by companies in their dealings with stakeholders in course of CCAA process.

Table of Authorities

Cases considered by *Pearlman J.*:

Cliffs Over Maple Bay Investments Ltd. v. Fisgard Capital Corp. (2008), 2008 BCCA 327, 2008 CarswellBC 1758, 83 B.C.L.R. (4th) 214, 296 D.L.R. (4th) 577, 434 W.A.C. 187, 258 B.C.A.C. 187, 46 C.B.R. (5th) 7, [2008] 10 W.W.R. 575 (B.C. C.A.) — distinguished

Encore Developments Ltd., Re (2009), 2009 BCSC 13, 2009 CarswellBC 84, 52 C.B.R. (5th) 30 (B.C. S.C.) — considered

Federal Gypsum Co., Re (2007), 2007 NSSC 347, 2007 CarswellNS 629, 261 N.S.R. (2d) 299, 40 C.B.R. (5th) 80, 835 A.P.R. 299 (N.S. S.C.) — considered

Hongkong Bank of Canada v. Chef Ready Foods Ltd. (1990), 51 B.C.L.R. (2d) 84, 1990 CarswellBC 394, 4 C.B.R. (3d) 311, (sub nom. *Chef Ready Foods Ltd. v. Hongkong Bank of Canada)* [1991] 2 W.W.R. 136 (B.C. C.A.) — considered

Pacific National Lease Holding Corp., Re (August 17, 1992), Doc. A922870 (B.C. S.C.) — followed

San Francisco Gifts Ltd., Re (2005), 2005 ABQB 91, 2005 CarswellAlta 174, 10 C.B.R. (5th) 275, 42 Alta. L.R. (4th) 377, 378 A.R. 361 (Alta. Q.B.) — distinguished

Ted Leroy Trucking Ltd., Re (2010), (sub nom. *Century Services Inc. v. Canada (A.G.))* [2010] 3 S.C.R. 379, [2010] G.S.T.C. 186, 12 B.C.L.R. (5th) 1, (sub nom. *Century Services Inc. v. A.G. of Canada)* 2011 G.T.C. 2006 (Eng.), (sub nom. *Century Services Inc. v. A.G. of Canada)* 2011 D.T.C. 5006 (Eng.), (sub nom. *Leroy (Ted) Trucking Ltd., Re)* 503 W.A.C. 1, (sub nom. *Leroy (Ted) Trucking Ltd., Re)* 296 B.C.A.C. 1, 2010 SCC 60, 2010 CarswellBC 3419, 2010 CarswellBC 3420, 409 N.R. 201, (sub nom. *Ted LeRoy Trucking Ltd., Re)* 326 D.L.R. (4th) 577, 72 C.B.R. (5th) 170, [2011] 2 W.W.R. 383 (S.C.C.) — considered

Statutes considered:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

s. 11.02(2) [en. 2005, c. 47, s. 128] — considered

s. 11.02(3) [en. 2005, c. 47, s. 128] — considered

s. 36 — referred to

APPLICATION by debtor companies for extension of stay under *Companies' Creditors Arrangement Act.*

***Pearlman J.*:**

Introduction

1 On December 16, 2011, on the application of the petitioners, I granted an order confirming and extending the Initial Order and stay pronounced June 6, 2011, and subsequently confirmed and extended to December 16, 2011, by a further 119 days to April 13, 2012. When I made the order, I informed counsel that I would provide written Reasons for Judgment. These are my Reasons.

Positions of the Parties

2 The petitioners apply for the extension of the Initial Order to April 13, 2012 in order to permit them additional time to work toward a plan of arrangement by continuing the marketing of the Vessel "QE014226C010" (the "Vessel") with Fraser Yachts, to explore potential Debtor In Possession ("DIP") financing to complete construction of the Vessel pending a sale, and to resolve priorities among *in rem* claims against the Vessel.

3 The application of the petitioners for an extension of the Initial Order and stay was either supported, or not opposed, by all of the creditors who have participated in these proceedings, other than the respondent, Harry Sargeant III.

4 The Monitor supports the extension as the best option available to all of the creditors and stakeholders at this time.

5 These proceedings had their genesis in a dispute between the petitioner Worldspan Marine Inc. and Mr. Sargeant. On February 29, 2008, Worldspan entered into a Vessel Construction Agreement with Mr. Sargeant for the construction of the Vessel, a 144-foot custom motor yacht. A dispute arose between Worldspan and Mr. Sargeant concerning the cost of construction. In January 2010 Mr. Sargeant ceased making payments to Worldspan under the Vessel Construction Agreement.

6 The petitioners continued construction until April 2010, by which time the total arrears invoiced to Mr. Sargeant totalled approximately $4.9 million. In April or May 2010, the petitioners ceased construction of the Vessel and the petitioner Queenship laid off 97 employees who were then working on the Vessel. The petitioners maintain that Mr. Sargeant's failure to pay monies due to them under the Vessel Construction Agreement resulted in their insolvency, and led to their application for relief under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, ("*CCAA*") in these proceedings.

7 Mr. Sargeant contends that the petitioners overcharged him. He claims against the petitioners, and against the as yet unfinished Vessel for the full amount he paid toward its construction, which totals $20,945,924.05.

8 Mr. Sargeant submits that the petitioners are unable to establish that circumstances exist that make an order extending the Initial Order appropriate, or that they have acted and continue to act in good faith and with due diligence. He says that the petitioners have no prospect of presenting a viable plan of arrangement to their creditors. Mr. Sargeant also contends that the petitioners have shown a lack of good faith by failing to disclose to the Court that the two principals of Worldspan, Mr. Blane, and Mr. Barnett are engaged in a dispute in the United States District Court for the Southern District of Florida where Mr. Barnett is suing Mr. Blane for fraud, breach of fiduciary duty and conversion respecting monies invested in Worldspan.

9 Mr. Sargeant drew the Court's attention to Exhibit 22 to the complaint filed in the United States District Court by Mr. Barnett, which is a demand letter dated June 29, 2011 from Mr. Barnett's Florida counsel to Mr. Blane stating:

> Your fraudulent actions not only caused monetary damage to Mr. Barnett, but also caused tremendous damage to WorldSpan. More specifically, your taking Mr. Barnett's money for your own use deprived the company of much needed capital. Your harm to WorldSpan is further demonstrated by your conspiracy with the former CEO of WorldSpan, Lee Taubeneck, to overcharge a customer in order to offset the funds you were stealing from Mr. Barnett that should have gone to the company. Your deplorable actions directly caused the demise of what could have been a successful and innovative new company" (underlining added)

10 Mr. Sargeant says, and I accept, that he is the customer referred to in the demand letter. He submits that the allegations contained in the complaint and demand letter lend credence to his claim that Worldspan breached the Vessel Construction Agreement by engaging in dishonest business practices, and over-billed him. Further, Mr. Sargeant says that the petitioner's failure to disclose this dispute between the principals of Worldspan, in addition to demonstrating a lack of good faith, reveals an internal division that diminishes the prospects of Worldspan continuing in business.

11 As yet, there has been no judicial determination of the allegations made by Mr. Barnett in his complaint against Mr. Blane.

Discussion and Analysis

12 On an application for an extension of a stay pursuant to s. 11.02(2) of the *CCAA*, the petitioners must establish that they have met the test set out in s. 11.02(3):

> (a) whether circumstances exist that make the order appropriate; and
>
> (b) whether the applicant has acted, and is acting, in good faith and with due diligence.

13 In considering whether "circumstances exist that make the order appropriate", the court must be satisfied that an extension of the Initial Order and stay will further the purposes of the *CCAA*.

14 In *Ted Leroy Trucking Ltd., Re*, [2010] 3 S.C.R. 379 (S.C.C.) at para. 70, Deschamps J., for the Court, stated:

> ... Appropriateness under the CCAA is assessed by inquiring whether the order sought advances the policy objectives underlying the CCAA. The question is whether the order will usefully further efforts to achieve the remedial purpose of the CCAA — avoiding the social and economic losses resulting from liquidation of an insolvent company. I would add that appropriateness extends not only to the purpose of the order, but also to the means it employs. Courts should be mindful that chances for successful reorganizations are enhanced where participants achieve common ground and all stakeholders are treated as advantageously and fairly as the circumstances permit.

15 A frequently cited statement of the purpose of the *CCAA* is found in *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 51 B.C.L.R. (2d) 84, [1990] B.C.J. No. 2384 (B.C. C.A.), at p. 3 where the Court of Appeal held:

> The purpose of the C.C.A.A. is to facilitate the making of a compromise or arrangement between an insolvent debtor company and its creditors to the end that the company is able to continue in business. It is available to any company incorporated in Canada with assets or business activities in Canada that is not a bank, a railway company, a telegraph company, an insurance company, a trust company, or a loan company. When a company has recourse to the C.C.A.A. the court is called upon to play a kind of supervisory role to preserve the status quo and to move the process along to the point where a compromise or arrangement is approved or it is evident that the attempt is doomed to failure. Obviously time is critical. Equally obviously, if the attempt at compromise or arrangement is to have any prospect of success there must be a means of holding the creditors at bay, hence the powers vested in the court under s. 11.

16 In *Pacific National Lease Holding Corp., Re*, [1992] B.C.J. No. 3070 (B.C. S.C.) Brenner J. (as he then was) summarized the applicable principles at para. 26:

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

17 In *Cliffs Over Maple Bay Investments Ltd. v. Fisgard Capital Corp.*, 2008 BCCA 327 (B.C. C.A.), the Court of Appeal set aside the extension of a stay granted to the debtor property development company. There, the Court held that the *CCAA* was not intended to accommodate a non-consensual stay of creditors' rights while a debtor company attempted to carry out a

restructuring plan that did not involve an arrangement or compromise on which the creditors could vote. At para. 26, Tysoe J.A., for the Court said this:

> In my opinion, the ability of the court to grant or continue a stay under s. 11 is not a free standing remedy that the court may grant whenever an insolvent company wishes to undertake a "restructuring", a term with a broad meaning including such things as refinancings, capital injections and asset sales and other downsizing. Rather, s. 11 is ancillary to the fundamental purpose of the *CCAA*, and a stay of proceedings freezing the rights of creditors should only be granted in furtherance of the *CCAA*'s fundamental purpose.

18 At para. 32, Tysoe J.A. queried whether the court should grant a stay under the *CCAA* to permit a sale, winding up or liquidation without requiring the matter to be voted upon by the creditors if the plan or arrangement intended to be made by the debtor company simply proposed that the net proceeds from the sale, winding up or liquidation be distributed to its creditors.

19 In *Cliffs Over Maple Bay Investments Ltd.* at para. 38, the court held:

> ... What the Debtor Company was endeavouring to accomplish in this case was to freeze the rights of all of its creditors while it undertook its restructuring plan without giving the creditors an opportunity to vote on the plan. The *CCAA* was not intended, in my view, to accommodate a non-consensual stay of creditors' rights while a debtor company attempts to carry out a restructuring plan that does not involve an arrangement or compromise upon which the creditors may vote.

20 As counsel for the petitioners submitted, *Cliffs Over Maple Bay Investments Ltd.* was decided before the current s. 36 of the *CCAA* came into force. That section permits the court to authorize the sale of a debtor's assets outside the ordinary course of business without a vote by the creditors.

21 Nonetheless, *Cliffs Over Maple Bay Investments Ltd.* is authority for the proposition that a stay, or an extension of a stay should only be granted in furtherance of the *CCAA*'s fundamental purpose of facilitating a plan of arrangement between the debtor companies and their creditors.

22 Other factors to be considered on an application for an extension of a stay include the debtor's progress during the previous stay period toward a restructuring; whether creditors will be prejudiced if the court grants the extension; and the comparative prejudice to the debtor, creditors and other stakeholders in not granting the extension: *Federal Gypsum Co., Re*, 2007 NSSC 347, 40 C.B.R. (5th) 80 (N.S. S.C.) at paras. 24-29.

23 The good faith requirement includes observance of reasonable commercial standards of fair dealings in the *CCAA* proceedings, the absence of intent to defraud, and a duty of honesty to the court and to the stakeholders directly affected by the *CCAA* process: *San Francisco Gifts Ltd., Re*, 2005 ABQB 91 (Alta. Q.B.) at paras. 14-17.

Whether circumstances exist that make an extension appropriate

24 The petitioners seek the extension to April 13, 2012 in order to allow a reasonable period of time to continue their efforts to restructure and to develop a plan of arrangement.

25 There are particular circumstances which have protracted these proceedings. Those circumstances include the following:

(a) Initially, Mr. Sargeant expressed an interest in funding the completion of the Vessel as a Crescent brand yacht at Worldspan shipyards. On July 22, 2011, on the application of Mr. Sargeant, the Court appointed an independent Vessel Construction Officer to prepare an analysis of the cost of completing the Vessel to Mr. Sargeant's specifications. The Vessel Construction Officer delivered his completion cost analysis on October 31, 2011.

(b) The Vessel was arrested in proceedings in the Federal Court of Canada brought by Offshore Interiors Inc., a creditor and a maritime lien claimant. As a result, The Federal Court, while recognizing the jurisdiction of this Court in the *CCAA* proceedings, has exercised its jurisdiction over the vessel. There are proceedings underway in the Federal Court for the determination of *in rem* claims against the Vessel. Because this Court has jurisdiction in the CCAA proceedings, and the Federal Court exercises its maritime law jurisdiction over the Vessel, there have been applications in both Courts with respect to the marketing of the Vessel.

(c) The Vessel, which is the principal asset of the petitioner Worldspan, is a partially completed custom built super yacht for which there is a limited market.

26 All of these factors have extended the time reasonably required for the petitioners to proceed with their restructuring, and to prepare a plan of arrangement.

27 On September 19, 2011, when this court confirmed and extended the Initial Order to December 16, 2011, it also authorized the petitioners to commence marketing the Vessel unless Mr. Sargeant paid $4 million into his solicitor's trust account on or before September 29, 2011.

28 Mr. Sargeant failed to pay the $4 million into trust with his solicitors, and subsequently made known his intention not to fund the completion of the Vessel by the petitioners.

29 On October 7, 2011, the Federal Court also made an order authorizing the petitioners to market the Vessel and to retain a leading international yacht broker, Fraser Yachts, to market the Vessel for an initial term of six months, expiring on April 7, 2012. Fraser Yachts has listed the Vessel for sale at $18.9 million, and is endeavouring to find a buyer. Although its efforts have attracted little interest to date, Fraser Yachts have expressed confidence that they will be able to find a buyer for the Vessel during the prime yacht buying season, which runs from February through July. Fraser Yachts and the Monitor have advised that process may take up to 9 months.

30 On November 10, 2011, this Court, on the application of the petitioners, made an order authorizing and approving the sale of their shipyard located at 27222 Lougheed Highway, with a leaseback of sufficient space to enable the petitioners to complete the construction of the Vessel, should they find a buyer who wishes to have the Vessel completed as a Crescent yacht at its current location. The sale and leaseback of the shipyard has now completed.

31 Both this Court and the Federal Court have made orders regarding the filing of claims by creditors against the petitioners and the filing of *in rem* claims in the Federal Court against the Vessel.

32 The determination of the *in rem* claims against the Vessel is proceeding in the Federal Court.

33 After dismissing the *in rem* claims of various creditors, the Federal Court has determined that the creditors having *in rem* claims against the Vessel are:

Sargeant	$20,945.924.05
Capri Insurance Services	$ 45,573.63
Cascade Raider	$ 64,460.02
Arrow Transportation and CCY	$ 50,000.00
Offshore Interiors Inc.	$659,011.85
Continental Hardwood Co.	$ 15,614.99
Paynes Marine Group	$ 35,833.17
Restaurant Design and Sales LLC	$254,383.28

34 The petitioner, Worldspan's, *in rem* claim in the amount of $6,643,082.59 was dismissed by the Federal Court and is currently subject to an appeal to be heard January 9, 2012.

35 In addition, Comerica Bank has asserted an *in rem* claim against the Vessel for $9,429,913.86, representing the amount it advanced toward the construction of the Vessel. Mr. Mohammed Al-Saleh, a judgment creditor of certain companies controlled by Mr. Sargeant has also asserted an *in rem* claim against the Vessel in the amount of $28,800,000.

36 The Federal Court will determine the validity of the outstanding *in rem* claims, and the priorities amongst the *in rem* claims against the Vessel.

37 The petitioners, in addition to seeking a buyer for the Vessel through Fraser Yachts are also currently in discussions with potential DIP lenders for a DIP facility for approximately $10 million that would be used to complete construction of the Vessel in the shipyard they now lease. Fraser Yachts has estimated that the value of the Vessel, if completed as a Crescent brand yacht at the petitioners' facility would be $28.5 million. If the petitioners are able to negotiate a DIP facility, resumption of construction of the Vessel would likely assist their marketing efforts, would permit the petitioners to resume operations, to generate cash flow and to re-hire workers. However, the petitioners anticipate that at least 90 days will be required to obtain a DIP facility, to review the cost of completing the Vessel, to assemble workers and trades, and to bring an application for DIP financing in both this Court and the Federal Court.

38 An extension of the stay will not materially prejudice any of the creditors or other stakeholders. This case is distinguishable from *Cliffs Over Maple Bay Investments Ltd.*, where the debtor was using the *CCAA* proceedings to freeze creditors' rights in order to prevent them from realizing against the property. Here, the petitioners are simultaneously pursuing both the marketing of the Vessel and efforts to obtain DIP financing that, if successful, would enable them to complete the construction of the Vessel at their rented facility. While they do so, a court supervised process for the sale of the Vessel is underway.

39 Mr. Sargeant also relies on *Encore Developments Ltd., Re*, 2009 BCSC 13 (B.C. S.C.), in support of his submission that the Court should refuse to extend the stay. There, two secure creditors applied successfully to set aside an Initial Order and stay granted *ex parte* to the debtor real estate development company. The debtor had obtained the Initial Order on the basis that it had sufficient equity in its real estate projects to fund the completion of the remaining projects. In reality, the debtor company had no equity in the projects, and at the time of the application the debtor company had no active business that required the protection of a *CCAA* stay. Here, when the petitioners applied for and obtained the Initial Order, they continued to employ a skeleton workforce at their facility. Their principal asset, aside from the shipyard, was the partially constructed Vessel. All parties recognized that the *CCAA* proceedings afforded an opportunity for the completion of the Vessel as a custom Crescent brand yacht, which represented the best way of maximizing the return on the Vessel. On the hearing of this application, all of the creditors, other than Mr. Sargeant share the view that the Vessel should be marketed and sold through and orderly process supervised by this Court and the Federal Court.

40 I share the view of the Monitor that in the particular circumstances of this case the petitioners cannot finalize a restructuring plan until the Vessel is sold and terms are negotiated for completing the Vessel either at Worldspan's rented facility, or elsewhere. In addition, before the creditors will be in a position to vote on a plan, the amounts and priorities of the creditors' claims, including the *in rem* claims against the Vessel, will need to be determined. The process for determining the *in rem* claims and their priorities is currently underway in the Federal Court.

41 The Monitor has recommended the Court grant the extension sought by the petitioners. The Monitor has raised one concern, which relates to the petitioners' current inability to fund ongoing operating costs, insurance, and professional fees incurred in the continuation of the *CCAA* proceedings. At this stage, the landlord has deferred rent for the shipyard for six months until May 2012. At present, the petitioners are not conducting any operations which generate cash flow. Since the last come back hearing in September, the petitioners were able to negotiate an arrangement whereby Mr. Sargeant paid for insurance coverage on the Vessel. It remains to be seen whether Mr. Sargeant, Comerica Bank, or some other party will pay the insurance for the Vessel which comes up for renewal in January, 2012.

42 Since the sale of the shipyard lands and premises, the petitioners have no assets other than the Vessel capable of protecting an Administration Charge. The Monitor has suggested that the petitioners apply to the Federal Court for an Administration Charge against the Vessel. Whether the petitioners do so is of course a matter for them to determine.

43 The petitioners will need to make arrangements for the continuing payment of their legal fees and the Monitor's fees and disbursements.

44 The *CCAA* proceedings cannot be extended indefinitely. However, at this stage, a *CCAA* restructuring still offers the best option for all of the stakeholders. Mr. Sargeant wants the stay lifted so that he may apply for the appointment of Receiver and exercise his remedies against the Vessel. Any application by Mr. Sargeant for the appointment of a Receiver would be resisted by the other creditors who want the Vessel to continue to be marketed under the Court supervised process now underway.

45 There is still the prospect that through the *CCAA* process the Vessel may be completed by the petitioners either as a result of their finding a buyer who wishes to have the Vessel completed at its present location, or by negotiating DIP

financing that enables them to resume construction of the Vessel. Both the marine surveyor engaged by Comerica Bank and Fraser Yachts have opined that finishing construction of the Vessel elsewhere would likely significantly reduce its value.

46 I am satisfied that there is a reasonable possibility that the petitioners, working with Fraser Yachts, will be able to find a purchaser for the Vessel before April 13, 2012, or that alternatively they will be able to negotiate DIP financing and then proceed with construction. I find there remains a reasonable prospect that the petitioners will be able to present a plan of arrangement to their creditors. I am satisfied that it is their intention to do so. Accordingly, I find that circumstances do exist at this time that make the extension order appropriate.

Good faith and due diligence

47 Since the last extension order granted on September 19, 2011, the petitioners have acted diligently by completing the sale of the shipyard and thereby reducing their overheads; by proceeding with the marketing of the Vessel pursuant to orders of this Court and the Federal Court; and by embarking upon negotiations for possible DIP financing, all in furtherance of their restructuring.

48 Notwithstanding the dispute between Mr. Barnett and Mr. Blane, which resulted in the commencement of litigation in the State of Florida at or about the same time this Court made its Initial Order in the *CCAA* proceedings, the petitioners have been able to take significant steps in the restructuring process, including the sale of the shipyard and leaseback of a portion of that facility, and the applications in both this Court and the Federal Court for orders for the marketing of the Vessel. The dispute between Mr. Barnett and his former partner, Mr. Blane has not prevented the petitioners from acting diligently in these proceedings. Nor am I persuaded on the evidence adduced on this application that dispute would preclude the petitioners from carrying on their business of designing and constructing custom yachts, in the event of a successful restructuring.

49 While the allegations of misconduct, fraud and misappropriation of funds made by Mr. Barnett against Mr. Blane are serious, at this stage they are no more than allegations. They have not yet been adjudicated. The allegations, which are as yet unproven, do not involve dishonesty, bad faith, of fraud by the debtor companies in their dealings with stakeholders in the course of the *CCAA* process.

50 In my view, the failure of the petitioners to disclose the dispute between Mr. Barnett and Mr. Blane does not constitute bad faith in the *CCAA* proceedings or warrant the exercise of the Court's discretion against an extension of the stay.

51 This case is distinguishable from *San Francisco Gifts Ltd.*, where the debtor company had pleaded guilty to 9 counts of copyright infringement, and had received a large fine for doing so.

52 In *San Francisco Gifts Ltd.*, at paras 30 to 32, the Alberta Court of Queen's Bench acknowledged that a debtor company's business practices may be so offensive as to warrant refusal of a stay extension on public policy grounds. However, the court declined to do so where the debtor company was acting in good faith and with due diligence in working toward presenting a plan of arrangement to its creditors.

53 The good faith requirement of s. 11.02(3) is concerned primarily with good faith by the debtor in the *CCAA* proceedings. I am satisfied that the petitioners have acted in good faith and with due diligence in these proceedings.

Conclusion

54 The petitioners have met the onus of establishing that circumstances exist that make the extension order appropriate and that they have acted and are acting in good faith and with due diligence. Accordingly, the extension of the Initial Order and stay to April 13, 2012 is granted on the terms pronounced on December 16, 2011.

Application granted.

End of Document

TAB 3

2000 CarswellAlta 1584
Alberta Court of Queen's Bench

Rio Nevada Energy Inc., Re

2000 CarswellAlta 1584, [2000] A.J. No. 1596, 102 A.C.W.S. (3d) 18, 283 A.R. 146

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

In the Matter of Rio Nevada Energy Inc.

Romaine J.

Judgment: December 18, 2000
Docket: Calgary 0001-17463

Counsel: *Brian P. O'Leary*, *Alison Z.A. Campbell*, for Westcoast Capital Corporation
Peter Pastewka, *James Eamon*, for Rio Nevada Energy Inc.
Larry Boyd Robinson, for Joseph Dow and Ronald Antonio

Subject: Corporate and Commercial; Insolvency

Headnote

Corporations --- Arrangements and compromises — Under Companies' Creditors Arrangements Act — Arrangements — Effect of arrangement — Stay of proceedings

Table of Authorities

Cases considered by *Romaine J.*:

Bargain Harold's Discount Ltd. v. Paribas Bank of Canada (1992), 10 C.B.R. (3d) 23, 4 B.L.R. (2d) 306, 7 O.R. (3d) 362 (Ont. Gen. Div.) — applied

First Treasury Financial Inc. v. Cango Petroleums Inc. (1991), 3 C.B.R. (3d) 232, 78 D.L.R. (4th) 585, [1991] O.J. No. 429 (Ont. Gen. Div.) — distinguished

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

Nova Metal Products Inc. v. Comiskey (Trustee of) (1990), 1 C.B.R. (3d) 101, (sub nom. *Elan Corp. v. Comiskey)* 1

O.R. (3d) 289, (sub nom. *Elan Corp. v. Comiskey)* 41 O.A.C. 282 (Ont. C.A.) — considered

Pacific National Lease Holding Corp., Re (August 17, 1992), Doc. A922870 (B.C. S.C.) — considered

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

Sharp-Rite Technologies Ltd., Re, 2000 BCSC 122, [2000] B.C.J. No. 135 (B.C. S.C.) — considered

Starcom International Optics Corp., Re (1998), 3 C.B.R. (4th) 177 (B.C. S.C. [In Chambers]) — considered

Statutes considered:

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

s. 11(3) — considered

s. 11(6) — considered

APPLICATION by creditor for order terminating stay of proceedings; CROSS-APPLICATION by debtor for order extending stay of proceedings.

***Romaine J.*:**

Introduction

1 Rio Nevada Energy Inc. sought, and obtained, protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c.C-36 on October 31, 2000. Rio Nevada's principal creditor, Westcoast Capital Corporation, declared its intention at that time to bring an application for an order terminating the stay of proceedings granted under the CCAA order on the basis that any plan of arrangement proposed by Rio Nevada would be "doomed to failure". The stay of proceedings under the order was initially extended to November 17, 2000. On that date, Westcoast applied for an order terminating the stay and appointing a receiver-manager of the assets of Rio Nevada pursuant to Westcoast's security. Rio Nevada applied for an order extending the stay to December 17, 2000, and amending certain provisions of the initial order. I dismissed Westcoast's application and extended the stay under the initial order to December 15, 2000. These are the reasons for my decision.

Facts

2 Rio Nevada is a publicly listed oil and gas company incorporated under the laws of Canada. In September, 1999, Rio Nevada entered into a prepaid gas purchase contract with Westcoast pursuant to which Rio Nevada was to deliver certain daily volumes of natural gas commencing in September, 1999 and ending on October 31, 2004. Westcoast prepaid $3,118,000 plus GST to Rio Nevada in accordance with the terms of the gas purchase contract.

3 As security under the gas purchase contract, Rio Nevada granted Westcoast a first ranking security interest and charge over all its assets. Upon default by Rio Nevada, Westcoast becomes able to appoint, or apply to the court to appoint, a receiver.

4 Rio Nevada had some difficulty with two new wells drilled to meet the gas production requirements of the gas purchase contract in that it has not been able to complete remedial work that would put these wells into production. Currently, the completion of remedial work on these wells awaits sufficient cold weather to allow access to them.

5 Rio Nevada had gas production shortfalls from time to time during the term of the gas purchase contract, which it cured by purchasing gas from a gas marketer and delivering it to Westcoast to satisfy its contractual obligations. Rio Nevada also acquired the shares of a manufacturing and research and development firm, Concorde Technologies Inc. (which included the acquisition of the shares of Tierra Industries Ltd.) and granted security on its assets as part of the financing of this acquisition. Westcoast considers this acquisition without its consent to be a breach of its security interest over the assets of Rio Nevada. On October 23, 2000, Westcoast terminated the gas purchase contract and claimed liquidated damages. Westcoast indicated its intention to take steps to appoint a receiver of the assets of Rio Nevada in the event payment was not received within 10 days.

6 Westcoast claims approximately $5,530,832 in liquidated damages under the gas purchase contract against Rio Nevada. Rio Nevada's liabilities to Westcoast and other secured, unsecured and statutory creditors aggregate approximately $10.6 million.

7 Outtrim Szaba Associates Ltd., a petroleum engineering evaluations firm, has estimated the fair market value of Rio Nevada's oil and natural gas assets at $9,427,000 as at November 13, 2000. This estimate is based on an evaluation of Rio Nevada's reserves and cash flow as of the same date.

8 Rio Nevada's aggregate liabilities of $10.6 million include debt from its acquisition of the shares of Concorde and Tierra. No evidence of the value of these shares is before the Court, but their purchase price in August, 2000 was approximately $5.25 million. Rio Nevada has additional miscellaneous assets worth approximately $250,000.

Issues

9

1) Should the stay of proceedings granted in the initial order be terminated because any plan of arrangement put forward by Rio Nevada is "deemed to failure"?

2) Should the stay granted under the initial order be extended?

Analysis

10 There is some disagreement between the parties as to the appropriate process to be followed in deciding these issues. Rio Nevada takes the position that the appropriate test is set out in Section 11(6) of the CCAA[1], and that the case law relating to the appropriate test in a "doomed to failure" application is merely a factor in applying Section 11(6): *Starcom International Optics Corp., Re* (1998), 3 C.B.R. (4th) 177 (B.C. S.C. [In Chambers]) at paragraph 22. Westcoast submits that, while Section 11(6) sets out the correct test for Rio Nevada's application to extend the stay, the correct test for deciding whether its application to terminate the stay should succeed is the test set out in the case law.

11 The problem arises in part because much of the case law relating to applications to set aside a stay pre-dates the addition of Section 11(6) to the CCAA in 1997. However, although Section 11(6) applications to implement or extend a stay may often be met with opposition asserting that such a stay is doomed to failure, it is not necessary for these cross-applications to co-exist in every case. It is preferable to consider these issues separately in order to ensure the burden of proof on each applicant is applied appropriately, and the "doomed to failure" application should be considered first.

12 The burden of proof in setting aside a CCAA stay by establishing that any plan of arrangement is "doomed to failure" rests on the applicant wishing to have CCAA proceedings terminated, in this case, Westcoast: *Bargain Harold's Discount Ltd. v. Paribas Bank of Canada*[2]; *Philip's Manufacturing Ltd., Re*[3]

13 Rio Nevada does not have the burden of proving that a plan of arrangement put forward by it is not "doomed to failure". As commented by Doherty, J.A. in *Nova Metal Products Inc. v. Comiskey (Trustee of)*[4], the nature of CCAA proceedings is such that many plans of arrangement will involve "variables and contingencies which will make the plan's ultimate acceptability to the creditors and the Court very uncertain at the time the initial application is made". As a result, the debtor company does not bear the burden of establishing the likelihood of success from the outset. Although this is not Rio Nevada's initial application, it is only seventeen days into CCAA proceedings, and Rio Nevada has not yet proposed any firm or specific plan of arrangement.

14 To meet the test set out in Section 11(6) for extension of a stay, Rio Nevada has the onus of proof and must satisfy the Court that circumstances exist that make such an order appropriate and that it has acted in good faith and diligently.

15 *Should the stay of proceedings granted in the initial order be terminated because any plan of arrangement put forward by Rio Nevada is "doomed to failure"?*

16 There appear to be at least two standards applied by courts in previous cases in deciding whether a stay under the CCAA should be set aside on a "doomed to failure" basis.

17 One standard, adopted by the courts in British Columbia, requires the applicant creditor to lead evidence to establish that a debtor company's attempt at a plan of arrangement is indeed doomed to failure: *Philip's Manufacturing Ltd., Re* (*supra*) at page 28; *Sharp-Rite Technologies Ltd., Re*[5]. As pointed out by Douglas Knowles and Alec Zimmerman in "*Further Developments and Trends in the Companies' Creditors Arrangement Act*: 1992" (Insolvency Institute of Canada), this standard is extremely difficult for a creditor to satisfy, particularly in the early stages of CCAA proceedings. I prefer, and adopt, the test that appears to have been applied by Austin, J. in *Bargain Harold's Discount Ltd.* (*supra*), that to succeed, the applicant creditor must show that there is no reasonable chance that any plan would be accepted.

18 In this case, there is no issue that Westcoast is a secured creditor of Rio Nevada. Although there is some dispute over the amount of liquidated damages owing under the gas purchase contract, this amounts to a difference of about $125,000. There is an issue of whether GST can be claimed as part of contractual damages that may affect the amount of the claim. However, it appears from the evidence that Westcoast's claim is at least $4,922,936, plus a September gas payment of $113,069.59 plus GST and an October gas payment for the period to termination of the contract in an approximate amount of $63,000 plus GST.

19 Even taking into account the disputed amount of liquidated damages and the GST issue, Westcoast's claim is approximately $5,043,000, and accrues interest at between $55 - 57,000 per month.

20 Westcoast submits that the market value of $9.4 million assigned to Rio Nevada's oil and gas assets by Outtrim Szabo is too high, and questions the qualifications of Outtrim Szabo to give this valuation opinion. Westcoast estimates the value of Rio Nevada's assets at $5,667,000, which it apparently arrived at by adding the value of Rio Nevada's Proved Developed Producing and Proved Developed Non-Producing reserves as set out in Outtrim Szabo's report and discounting at 15%. Westcoast ascribes no value to Rio Nevada's Proved Undeveloped or Probable Additional reserves, nor any value to the Concorde and Tierra shares or Rio Nevada's other miscellaneous assets. There is no independent evidence before me that this is an appropriate evaluation methodology for this company or that Outtrim Szabo's opinion is not appropriate in the circumstances.

21 In support of its application to terminate the stay, Westcoast submits that its security position is being eroded on a daily basis, as Rio Nevada's reserves are being developed at a value of between $7,000 and $10,000 a day. Westcoast submits that this is a situation of depleting resources, that interest is accruing and that professional fees will be incurred as part of the CCAA proceedings. If there is a real risk that a creditor's loan will become unsecured during the stay period, this is a factor to be taken into account in determining whether there should be a termination of the stay: *Nova Metal Products Inc.* (*supra*). In this case, however, I am not satisfied on the valuation evidence that is before me that there is a substantial risk of encroachment on Westcoast's security. I am not satisfied that Westcoast's estimate of the value of Rio Nevada's assets should be preferred over the Outtrim Szabo opinion, nor that I should conclude at this point that no value should be ascribed to Rio Nevada's other assets. Assuming the market value of Rio Nevada's assets to be somewhere in a range between $5.6 million and $9.5 million, there is sufficient value and more to cover Westcoast's claim for the relatively brief period of the stay requested by Rio Nevada.

22 Westcoast also submits that Rio Nevada has had more than enough time to attempt a sale of assets or a restructuring, as it has been making efforts to resolve its financial problems since mid-August, 2000. However, Rio Nevada has had only seventeen days of protection under the CCAA, and the Monitor reports that Rio Nevada has had extensive discussions with potential purchasers and merger partners and is investigating the possibility of a re-financing. There is no suggestion of lack of diligence by Rio Nevada in attempting to formulate a reasonable reorganization plan.

23 The actual market value of Rio Nevada will be determined by its ability to restructure and to sell assets. Given the report of the Monitor, some potential exists for a plan of arrangement to be proposed that will cover the Westcoast debt and other creditors, or perhaps even leave an operating company with value to cover other secured and unsecured debt and preserve the interests of non-creditor constituencies.

24 Westcoast submits that the value of Rio Nevada's reserves has deteriorated significantly from the date of its previous reserve report, May, 2000. However, given the relatively short stay period that is currently being requested, there is no

evidence that the value of the reserves will continue to deteriorate to any great extent.

25 Finally, Westcoast says that it has lost confidence in the management of Rio Nevada and would be unable to support a plan of arrangement put forward by it. There is, however, some evidence that Westcoast will not act against its commercial interest and that it will act reasonably in considering proposals put to it by Rio Nevada. As pointed out by Holmes, J. in *Sharp-Rite Technologies, Re* (*supra*), this type of submission by a creditor during a "doomed to failure" application must be viewed with some skepticism, since commercial reality may dictate a change of position when the details of a plan of arrangement have been presented. This is not a case such as *First Treasury Financial Inc. v. Cango Petroleums Inc.*[6], where all the creditors, secured and unsecured, have lost confidence in current management, or where it is highly probably than any plan put forward would be defeated by all the creditors.

26 It is appropriate to consider all affected parties in an application of this kind, including other secured and unsecured creditors: *Bargain Harold's* (*supra*) at paragraph 35. Here, the remaining two secured creditors support the application for a stay, on the basis that if there is value in Rio Nevada, the CCAA proceedings are most likely to allow all creditors to realize on their positions.

27 Taking into account all of the submissions and evidence, I am not satisfied that there is no reasonable chance that a plan of arrangement would be accepted.

28 *Has Rio Nevada met the requirements of Section 11(6) of the CCAA such that the stay granted under Section 11(3) should be continued*?

29 Section 11(6) requires Rio Nevada to establish three conditions prior to obtaining an order continuing the stay. They are:

a) that circumstances exist that make the order appropriate;

b) that Rio Nevada has acted, and is acting, in good faith; and

c) that Rio Nevada has acted, and is acting, with due diligence.

30 The evidence of Rio Nevada's efforts to refinance the Westcoast debt has not been contested, and I have already stated that, given the relatively short period of the stay under the CCAA to the date of these applications, there has been no lack of due diligence in that regard.

31 The only evidence that may suggest lack of good faith by Rio Nevada is Westcoast's complaint that it was misled by Rio Nevada's management with respect to the status of well remediation, and also misled with respect to the acquisition of the shares of Concorde and Tierra. These are issues that relate more to Westcoast's decision to terminate the gas purchase contract than to Rio Nevada's conduct under CCAA proceedings, and are, at any event, in dispute between the parties. I am satisfied by the evidence put forward by Rio Nevada and by the Monitor that Rio Nevada has acted and is acting in good faith with respect to these proceedings.

32 As to whether circumstances exist that make the continuation of the stay appropriate, there are a number of factors that must be taken into account. The continuation of the stay in this case is supported by the basic purpose of the CCAA, to allow an insolvent company a reasonable period of time to reorganize and propose a plan of arrangement to its creditors and the court and to prevent manoeuvres for positioning among creditors in the interim; *Pacific National Lease Holding Corp., Re*[7]; *Meridian Development Inc. v. Toronto Dominion Bank*[8]. Westcoast has not satisfied the Court that an attempt at an acceptable compromise or arrangement is doomed to failure at this point in time. Negotiations for restructuring a sale or refinancing are ongoing, and there has been a strengthening of the management team. Rio Nevada continues in business, and plans are underway to remediate its two major wells, which will significantly increase the company's rate of production. A Monitor is in place, which provides comfort to the creditors that assets are not being dissipated and current operations are being supervised. The extension sought is not unduly long, and is supported by the secured creditors other than Westcoast. The costs of the CCAA proceedings are likely no less onerous than the costs of a receivership in these circumstances, and the relief sought under the CCAA less drastic to all constituencies than the order that would likely have to be made in a receivership.

33 I find that Rio Nevada has established that continuation of the stay is appropriate, and that the conditions to granting such an order have been met.

Application dismissed; cross-application granted.

Footnotes

1 11(6) *Burden of proof on application* - The court shall not make an order under subsection ... (4) [to extend a stay] unless
(a) the applicant satisfies the court that circumstances exist that make such an order appropriate; and

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

2 (1992), 10 C.B.R. (3d) 23 (Ont. Gen. Div.) at page 30.

3 (1992), 9 C.B.R. (3d) 25 (B.C. C.A.) at page 28.

4 (1990), 1 C.B.R. (3d) 101, 41 O.A.C. 282 (Ont. C.A.), (sub nom. *Elan Corp. v. Comiskey*) , at page 316.

5 [2000] B.C.J. No. 135 (B.C. S.C.) at paragraph 25

6 [1991] O.J. No. 429 (Ont. Gen. Div.)

7 (August 17, 1992), Doc. A922870 (B.C. S.C.)

8 [1984] 5 W.W.R. 215, 53 A.R. 39 (Alta. Q.B.)

TAB 4

Date: 20001201
Action No. 0003 19315

IN THE COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL DISTRICT OF EDMONTON

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

AND IN THE MATTER OF Hunters Trailer & Marine Ltd.

MEMORANDUM OF DECISION
OF THE HONOURABLE ALLAN H. WACHOWICH
ASSOCIATE CHIEF JUSTICE

APPEARANCES:

Michael J. McCabe
Reynolds Mirth Richards & Farmer

Kentigern A. Rowan
Ogilvie & Company

Darcy G. Readman
Duncan & Craig

Terrence M. Warner
Miller Thompson

John L. Ircandia
Borden Ladner Gervais LLP

Douglas H. Shell
Lucas Bowker & White

Jeremy Hockin
Parlee McLaws

Background

[1] Hunters Trailer & Marine Ltd. ("Hunters") applied for and was granted a stay of proceedings, *ex parte*, on October 11, 2000, pursuant to the *Companies Creditors' Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "*CCAA*"). The order permitted Hunters to carry on business in a manner consistent with the preservation of Hunters' business and property for 30

days, under the supervision of a court-appointed Monitor, and within the terms of the order. The order authorized "debtor in possession" ("DIP") financing up to $1.5 Million which would have "super-priority" status over any other claims. An Administration Charge of up to $1 Million was also granted, and was given priority over every other security except for the DIP financing.

[2] A short-term extension of the stay, to November 17, 2000, was granted by the Honourable Mr. Justice W.E. Wilson on November 8, 2000. His amendments to the original order included a reduction in the maximum amount available for DIP financing to $800,000.00, and a reduction in the maximum Administration Charge to $350,000.00.

Current Application

[3] Hunters seeks to extend the stay of proceedings to at least February 28, 2001. They also seek an increase in the maximum amount of DIP financing and Administrative Charge available. Three of Hunters' major creditors (the "Objecting Creditors"), who are floor plan financiers, oppose the applications. The Objecting Creditors are Deutsche Financial Services, the Bank of America Specialty Group Ltd. and C.I.T. Financial Ltd. Hunters owes them in excess of $2,000,000.00, $3,085,728.80, and $4,567,239.00 respectively. All three are first charge creditors, but it is not yet clear how they rank in terms of priority. Two other major creditors support Hunters' application for an extension. One is Canada Western Bank, whom Hunters owes $1,061,000.00 on a line of credit, and who is currently providing DIP financing. The other is U.M.C. Financial Management Inc., whom Hunters owes $3,400,000.00, principally secured by a real estate mortgage.

[4] The onus in a stay application under the *CCAA* is dictated by s. 11(6) of the *CCAA*:

> 11 (6) The court shall not make an order under subsection (3) or (4) unless
>
> (a) the applicant satisfies the court that circumstances exist that make such an order appropriate; and
>
> (b) in the case of an order under subsection (4), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

[5] In this case, it will be unnecessary to deal with subsection (b). In light of the evidence before me, I find that the applicant, Hunters, has not satisfied its onus of showing that a stay would be appropriate in the circumstances. In arriving at this conclusion, I considered two issues - first, whether DIP financing should continue, and second, whether the purpose of the *CCAA* would be achieved by granting an extension of the stay.

DIP Financing

[6] In *Re United Used Auto & Truck Parts Ltd.* (1999), 12 C.B.R. (4th) 144 (B.C.S.C.), Tysoe J. articulated the test for when DIP financing should be permitted: there must be cogent evidence that the benefit of DIP financing clearly outweighs the potential prejudice to the lenders whose security is being subordinated: p. 153, para. 28. In that case, Tysoe J. found that DIP financing

would benefit the business, but was not critical for the operation or restructuring of the business. As well, he did not have sufficient confidence in the cash flow projections and appraised value of the realty to conclude that the benefit clearly outweighed the potential prejudice to the secured lenders: p. 153, para. 29.

[7] This reasoning was not objected to on appeal: *Re United Used Auto & Truck Parts Ltd.* (2000), 16 C.B.R. (4th) 141 (B.C.C.A.). The issue in the appeal was whether the court has jurisdiction to grant priority to a monitor's fees and expenses. Mackenzie J.A., speaking for the Court, held that the court's jurisdiction is found in equity, as is its jurisdiction to order super-priority for DIP financing: p. 152, paras. 30-31. On the issue of when this priority should be granted, Mackenzie J.A. stated, at para. 30:

> It is a time honoured function of equity to adapt to new exigencies. At the same time it should not be overlooked that costs of administration and DIP financing can erode the security of creditors and *CCAA* orders should only be made if there is a reasonable prospect of a successful restructuring.

[8] Determining whether DIP financing is appropriate requires a careful balancing of interests.

[9] In *Re Royal Oak Mines Inc.* (1999), 6 C.B.R. (4th) 314 (Ont. Gen. Div.), Blair J. made the following comments at pp. 321-322, para. 24:

> It follows from what I have said that, in my opinion, extraordinary relief such as DIP financing with super priority status should be kept, in Initial Orders, to what is reasonably necessary to meet the debtor company's urgent needs over the sorting-out period. Such measures involve what may be a significant re-ordering of priorities from those in place before the application is made, not in the sense of altering the existing priorities as between the various secured creditors but in the sense of placing encumbrances ahead of those presently in existence. Such changes should not be imported lightly, if at all, into the creditors mix; and affected parties are entitled to a reasonable opportunity to think about their potential impact, and to consider such things as whether or not the CCAA approach to the insolvency is the appropriate one in the circumstances - as opposed, for instance. to a receivership or bankruptcy - and whether or not, or to what extent, they are prepared to have their positions affected by DIP or super priority financing. As Mr. Dunphy noted, in the context of this case, the object should be to "keep the lights [of the company] on" and enable it to keep up with appropriate preventative maintenance measures, but the Initial Order itself should approach that objective in a judicious and cautious matter.

[10] In my view, the evidence provided by Hunters does not show that the benefits of DIP financing will clearly outweigh potential prejudice to the Objecting Creditors. While DIP financing is the only means for Hunters to continue operating, it is impossible to conclude that this short-term benefit will culminate in Hunters' financial recovery, due to a number of deficiencies in the evidence. First, there are no appraisals of the real estate or rolling stock in evidence to support Hunters' financial projections. Second, because Hunters' computer services provider shut down Hunters' computer based accounting system, Hunters and the Monitor have

had extremely limited access to Hunters' books and records. As a result, final financial statements for the year ended February 29, 2000 are unavailable, and current, reliable balance sheets cannot be provided. The Monitor cannot verify Hunters' financial situation because reliable data cannot be accessed.

[11] Third, the value of a major asset is uncertain. According to Hunters, the insurance policies on the life of Mr. Bondar's father are worth $2,300,000.00, and security is held against them by the mortgagee of the lands to the extent of $1,800,000.00. However, the policies are not in evidence, so the value and terms are uncertain. Also, apparently Mr. Bondar's wife is a beneficiary, but the percentage of her interest is not in evidence.

[12] Fourth, Hunters' cashflow projections are not supported by evidence from the Monitor or any other independent third party, which would verify their reasonableness or accuracy. Already, it appears that the Monitor's fees will be $100,000.00 greater than the cashflow projections anticipated. In light of all of the above deficiencies in Hunters' evidence, Hunters has not satisfied its onus of showing that DIP financing would be beneficial, or indeed, that a stay would be appropriate in the circumstances.

[13] Another consideration in assessing the benefit of DIP financing is that even if Hunters' projected cashflows are accurate, they show a continuing net deficit, suggesting that the benefit of DIP financing is merely prolonging the inevitable. Even as of September 2001, following the months when the volume of Recreational Vehicle ("RV") sales is highest, Hunters expects a cash flow deficit. After September, the RV sales will slow down significantly as Hunters enters the low season, so cash flow is not likely to increase after September. Hunters can expect continuing difficulties in meeting operating expenses well into the foreseeable future. The sources of Hunters' cash flow problems, as identified by Blair Bondar, the company president, will likely continue to exist. Mr. Bondar states that RV sales have decreased as a result of, in part, increasing gas prices, a weak Canadian dollar, and increased competition. Hunters has no control over these systemic problems, and there is no evidence or reason to believe that they will be resolved in the foreseeable future. As a result, I am not convinced that the cash flow projections themselves are accurate. The Monitor does not verify the accuracy or reasonableness of the projections. Therefore, it is impossible to conclude that the DIP financing will benefit Hunters and its creditors in the long run.

[14] The prejudice caused by DIP financing to the Objecting Creditors could be significant. The Objecting Creditors hold Purchase Money Security Interests and therefore their claims rank ahead of all other creditors', but their ability to realize on this statute-granted priority will be reduced further every time increases in DIP financing and Administrative Charges are approved to fund Hunters' operating costs. Extending the stay until February, 2001 would place the Objecting Creditors at risk during a period when RV sales are very slow and minimal cash flow will be generated. In order for Hunters to carry on its business, further increases in DIP financing are inevitable. This financing, which has now exceeded $800,000.00 in order to cover payroll for November, and the Administrative Charges of $350,000, are eroding the security of the Creditors while the financial position of Hunters is precarious and uncertain. Given these circumstances, and the principle from *Re Royal Oak Mines Inc., supra.* that DIP financing and its super-priority should not be granted lightly, DIP financing is not appropriate. The potential prejudice of DIP financing to the Objecting Creditors is not outweighed by the benefit to Hunters, and there is insufficient evidence of a reasonable possibility of a successful restructuring.

Purpose of the *CCAA*

[15] I described the purpose of the *CCAA* in *Meridian Developments Inc. v. Toronto Dominion Bank* (1984), 52 C.B.R. (N.S.) 109 (Alta. Q.B.) as follows, at p. 114:

> The legislation is intended to have wide scope and allows a judge to make orders which will effectively maintain the status quo for a period while the insolvent company attempts to gain the approval of its creditors for a proposed arrangement which will enable the company to remain in operation for what is, hopefully, the future benefit of both the company and its creditors.

[16] In this case, an extension of the stay will not maintain the status quo for the Objecting Creditors. Their priority status and ability to recover their losses will be jeopardized. At least two of the Objecting Creditors have buy-back agreements with manufacturers that will be impaired or disappear with the passage of time. These Creditors could then only recover their costs if Hunters is able to sell all of this inventory at cost or higher, a prospect that appears to be unrealistic. The *CCAA* should not be used where, as in this case, it will put the financial well-being of the majority of the creditors at risk.

[17] Another factor influencing my decision is the possibility that the inventory that is not subject to buy-back agreements will decline in value over the period of the stay. The other creditors will not face a decline in their interests in real estate and DIP financing, and it would be unfair to maintain the status quo for these creditors while the interest of the Objecting Creditors deteriorates. Another circumstance that could result in prejudice to the Objecting Creditors is the requirement in the Order that 10% of the proceeds from the sale of the Creditors' collateral shall be paid to Hunters for operating costs. This reduces the security available to the Objecting Creditors, who are inventory suppliers, while Hunter endures the slow season in RV sales.

[18] A stay of proceedings should not be granted under the *CCAA* where it would only prolong the inevitable, or where the position of the objecting respondents would be unduly jeopardized: *Timber Lodge Ltd. v. All Creditors of Timber Lodge Ltd.* (1992), 15 C.B.R. (3d) 244 (P.E.I. S.C.T. D.) at p. 252, para. 21; p. 253, para. 24. The B.C. Court of Appeal said that *CCAA* orders should only be made if there is a reasonable prospect of a successful restructuring: *Re United Used Auto & Truck Parts Ltd.*, *supra.* at p. 152, para. 30. Given my conclusion that further DIP financing should not be permitted, it is clear that Hunters will be unable to finance its operating costs, and therefore the business is doomed to failure. But even if DIP financing continued, the problems with cashflow, discussed above, suggest that Hunters has no reasonable prospect of becoming viable again.

[19] The jurisprudence makes it clear that the objection of a few recalcitrant creditors should not prevent the petitioner from proceeding to attempt to work out a plan under the *CCAA*: *Icor Oil & Gas Co. v. Canadian Imperial Bank of Commerce* (1989), 102 A.R. 161 (Q.B.) at p. 164, para. 21. The court should consider the interests of all affected constituencies in deciding whether a stay is appropriate, including secured, preferred and unsecured creditors, employees, landlords, shareholders, and the public generally: *Bargain Harold's Discount Ltd. v. Paribas Bank of Canada* (1992), 7 O.R. (3d) 362 (Ont. Ct. G.D.) at p. 369.

[20] However, in *Bargain Harold's Discount*, *supra.*, Austin J. also stated that where no plan will be acceptable to the required percentage of creditors, the *CCAA* application should be

refused: p. 369. Put another way, one factor to be considered in the context of s. 11(6) is whether the attempt to reach a compromise is doomed to failure, or is a realistic ambition: *Re Starcom International Optics Corp.* (1998), 3 C.B.R. (4th) 177 (B.C.S.C.) at p. 184, para. 22. I am satisfied that in this case, no compromise will be reached between the Objecting Creditors and the other major secured creditors, nor between the Objecting Creditors and Hunters.

[21] For all of these reasons, Hunters' application for an extension of the stay of proceedings is denied. However, in order to allow creditors time to prepare, the effect of my dismissal of Hunters' application will be suspended for one week. Therefore, I order a short-term extension of the stay of proceedings to December 8, 2000.

HEARD on the 17th day of November, 2000.
DATED at Edmonton, Alberta this 1st day of December, 2000.

A.C.J.C.Q.B.A.

TAB 5

1992 CarswellOnt 159
Ontario Court of Justice (General Division), Commercial List

Bargain Harold's Discount Ltd. v. Paribas Bank of Canada

1992 CarswellOnt 159, [1992] O.J. No. 374, 10 C.B.R. (3d) 23, 32 A.C.W.S. (3d) 242, 4 B.L.R. (2d) 306, 7 O.R. (3d) 362

BARGAIN HAROLD'S DISCOUNT LIMITED v. PARIBAS BANK OF CANADA, QUEBEC EQUITY CAPITAL AND COMPANY, LIMITED PARTNERSHIP, 967471 ONTARIO LIMITED, CCFL HIGH YIELD FUND AND COMPANY, LIMITED PARTNERSHIP, K MART CANADA LIMITED, 967473 ONTARIO LIMITED and 967472 ONTARIO LIMITED

Re AN INTENDED ACTION: PARIBAS BANK OF CANADA v. BARGAIN HAROLD'S DISCOUNT LIMITED, ROYAL BANK OF CANADA, CCFL HIGH YIELD FUND and COMPANY, LIMITED PARTNERSHIP, and K MART CANADA LIMITED

Austin J.

Heard: February 26, 1992
Judgment: February 28, 1992
Docket: Doc. B49/92

Counsel: *Aubrey E. Kauffman*, for Bargain Harold's Discount Limited and Quebec Equity Capital and Company, Limited Partnership.
H. Lorne Morphy, Q.C., and *Richard Conway* for Paribas Bank of Canada.
C. Francis, for Royal Bank of Canada.
D.V. MacDonald, for CCFL High Yield Fund and Company, Limited Partnership and Royal Insurance Company of Canada.
K. McElcheran, for K Mart Canada Limited.

Subject: Corporate and Commercial; Insolvency

Headnote

Corporations --- Arrangements and compromises — Under Companies' Creditors Arrangements Act — Application of Act

Corporations — Arrangements and compromises — Companies' Creditors Arrangement Act — Application by debtor corporation for order under s. 11 opposed by several secured creditors — No reasonable prospect of debtor being able to devise acceptable plan — Opposing creditors satisfying burden of proof — Application dismissed — Receiver-manager appointed with power to make assignment in bankruptcy — Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.

The debtor corporation applied for an order under s. 11 of the *Companies' Creditors Arrangement Act* ("CCAA."). It was opposed by a number of secured creditors.

Held:

The application was dismissed.

The burden of proof to show why the application should or should not be granted was on the opposing creditors. The fact that the opposing creditors alleged that there was no plan that they would approve did not put an end to the matter. All affected constituencies must be considered, including secured, preferred and unsecured creditors, employees, landlords, shareholders and the public generally. Where it is obvious that no plan will be found acceptable by the required percentage of creditors, the application should be refused. There must be a reasonable chance that a plan will be accepted.

In this case, there was no reasonable prospect of the debtor corporation being able to devise a plan or arrangement which would meet the approval requirements of s. 6 of the CCAA. The debtor corporation did not know the precise nature of the problem which brought about its present financial circumstances. According to its own auditors, the cause or causes might never be known. The debtor corporation also had no specific idea as to how its operation could be salvaged, other than to suggest "downsizing". There was no reason to believe that a downsizing could be done any more efficiently by the debtor corporation than by a receiver. Furthermore, no source of funding to permit the debtor corporation to continue in business had been suggested and there was a complete loss of confidence by the creditors in the management of the debtor corporation.

The appointment of a receiver-manager was to be effective immediately. The receiver was to have power to make an assignment in bankruptcy should it be so advised. A major asset of the debtor corporation consisted of leases and a trustee in bankruptcy would have much wider powers to deal with leases than a receiver did.

Table of Authorities

Cases considered:

First Treasury Financial Inc. v. Cango Petroleums Inc. (1991), 3 C.B.R. (3d) 232 (Ont. Gen. Div.) — *applied*

Icor Oil & Gas Co. v. Canadian Imperial Bank of Commerce (1989), 102 A.R. 161 (Q.B.) — *referred to*

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

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

Statutes considered:

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

s. 3(a)

s. 6

s. 11

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

Application for order under s. 11 of *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36.

***Austin J.*:**

1 This is an application by Bargain Harold's Discount Limited for an order under s. 11 of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ["C.C.A.A."]. It is opposed by a number of secured creditors. Paribas is the first secured creditor in terms of priority. It has either com menced an action or intends to do so and in that action has brought a motion for the appointment of a receiver and manager.

2 Bargain Harold's is an Ontario corporation. It operates a chain of "convenience discount stores." There are presently 160 stores in Manitoba, Ontario, New Brunswick, Nova Scotia, Prince Edward Island and Newfoundland. One hundred and fourteen of the stores are in Ontario. All stores are in leased premises. There are about 1,600 full-time employees and 2,360 part-time employees.

3 Bargain Harold's was established in 1969. The business was acquired by K Mart in 1985. K Mart substantially increased the number of stores. Through a leveraged buy-out, ownership changed in October 1990. The shares are presently held 80 per cent by Quebec Equity, 10 per cent by CCFL and Royal Insurance, and 10 per cent by management.

4 As at December 28, 1991, based on unaudited internal draft financial statements, Bargain Harold's had current assets totalling $83,295,619, and fixed assets of $20,237,638, a total of $103,533,257.

5 The same sources showed the major secured creditors as follows:

1. Paribas	- $ 7,500,000
2. Royal Bank	- $ 8,100,000
3. CCFL/RICC	- $ 29,500,000
4. K Mart	- $ 12,000,000
Total	- $ 57,100,000

6 By January 31, 1992, again based on internal data, the debt to Paribas had decreased to $5,000,000 and the debt to the Royal Bank had increased to $13,500,000, making the total overall $60,000,000.

7 Unaudited internal records indicated that as at December 28, 1991, the unsecured creditors and equipment lessors were as follows:

1. Trade Creditors	-	$51,782,000
2. Capital Equipment Lease Obligations	-	$ 4,227,000
3. Others	-	$16,811,000
Total	-	$72,820,000

8 It is admitted by the applicant that its financial situation has deteriorated since December 28, 1991.

9 During the period October 1990 to December 1991, the new owners instituted a program of store reformatting and acquired computerized point-of-sale systems with centralized computer facilities. These, with other capital expenditures, cost a total of $15,000,000. According to the uncontradicted evidence, this was some $7,000,000 in excess of what was permitted by the applicant's arrangement with Paribas.

10 According to the applicant, its "immediate financial difficulties" arise from five sources:

(1)the $15,000,000 expenditure;

(2)undetected errors in the management information system;

(3)excess inventory building due to reduced sales;

(4)inadequate analysis of financial data relating to operating margins; and

(5)external economic conditions.

11 The detail provided indicates that subsequent to June 30, 1991, management relied heavily on its new information system. Bargain Harold's fiscal year end is December 31. It was not until the year-end audit, which is still in progress, that it was discovered that the gross margin on sales for the second half of fiscal 1991 was lower than that which management believed had been achieved and was projecting. From July 1991 on, management conducted its affairs and recorded its results on the basis of erroneous gross market assumptions. This led to the acquisition of excess inventory. The situation was aggravated by the increasingly poor retail market.

12 One result of this admitted mismanagement is that the applicant has defaulted in principal payments of $11,500,000, together with interest, owing to CCFL/RICC. The applicant is also making payments to trade suppliers on an extended basis and certain suppliers are refusing to ship further inventory. There is insufficient working capital to pay obligations as they become due.

13 The purchase of the business in 1990 was financed in part by a revolving line of credit in the amount of $7,500,000 provided by Paribas. The Royal Bank provided a similar line in the amount of $20,000,000. In the fourth quarter of 1991, the applicant's relationship with Paribas and the Royal Bank deteriorated markedly. Effective January 1, 1992, Paribas reduced its credit facility from $7,500,000 to $5,000,000 and the Royal Bank reduced its credit facility from $20,000,000 to $15,000,000. The Royal Bank's position is guaranteed by K Mart.

14 In October 1991, an attempt was made to raise $15,000,000 in equity. According to the applicant, this was to finance further expansion. Again, according to the applicant, when its accounting and financial problems were discovered this attempt was abandoned. According to the evidence of Paribas, Bargain Harold's financial agents had discussions with potential purchasers in various cities, including Toronto, Montreal, Winnipeg, and New York. They were not successful.

15 The applicant has been negotiating with some or all of the secured creditors for some time, weeks if not months. Until very recently, K Mart was prepared to advance a further $5,000,000 under certain conditions. That arrangement fell through on February 19. On February 20, the applicant issued debentures of $100 each to each of 967471 Ontario Limited and 967472 Ontario Limited in order to qualify under s. 3(*a*) of the C.C.A.A. No issue is taken with these "instant" debentures.

16 On February 21, 1992, the Royal Bank demanded payment in full by March 6. K Mart has indicated its intention to honour its guarantee. On February 21, 1992, Paribas demanded payment in full by March 13.

17 No specific plan is put forward. Counsel for Paribas was critical of the applicant in this regard. The applicant's response was that negotiations with creditors had broken down so recently that there simply was no time to prepare a plan. There may be some merit in that response.

18 Evidence from Paribas states that at the time of the purchase in 1990, it was widely recognized that Bargain Harold's was not and had not been profitable. Whether the business was profitable in the period October 1990 to June 30, 1991, and if so, to what degree, is not revealed in the material filed. It may be that that is simply unknown.

19 As of October 2, 1991, Bargain Harold's was predicting a half-a-million-dollar profit for 1991. On October 3, that figure was changed to a loss of $3 to $4 million, on October 8, to a loss of $2.2 million, on November 14, to a loss of $4 million, on December 6, to a loss of $8 million, and on February 19, to a loss of $20 million.

20 Of particular significance is the following paragraph from the affidavit of Michael Gosselin of Paribas:

> On February 20, 1992, I met with representatives of Coopers & Lybrand to attempt to obtain an accounting of the loss. It was suggested to me that up to $7,000,000 of the additional $12,000,000 loss might be attributable to a defect in the recording of proper margins on goods sold which were undetected by management for six months. However, the auditors could not confirm that this was the cause of this unanticipated loss and, more importantly, stated that they might never be in a position to unequivocally confirm the causes. The remaining $5,000,000 loss could not be explained at all by Coopers & Lybrand who advised that their forensic accountants have been asked by CCFL and QECC to investigate the situation.

Coopers & Lybrand were the applicant's auditors. Translated to another medium, this language suggests that the patient is bleeding to death, but the doctors are unable to determine why.

21 It must be kept in mind that this affidavit was sworn February 26 and, as with so many of these applications, there has been no opportunity for cross-examination although an affidavit was filed in response to Gosselin's.

22 All that the applicant suggests is that it proposes to "downsize its business operation generally." In his submissions, counsel for the applicant pointed to Quebec Equity and to CCFL as substantial shareholders and potential sources of financing. Although both of those respondents supported the application, no commitment of any kind was forthcoming from either of them.

23 The applicant itself proposed the appointment of a monitor. The nominee was Price Waterhouse Limited. In this regard, counsel for the two sides had co-ordinated their efforts and it was agreed that in the event a receiver was appointed, either now or later, it should be Price Waterhouse. This makes a good deal of sense in terms of continuity and cost.

24 The applicant proposed a relatively detailed scheme of administration and monitorship. The applicant also proposed a very short time, i.e., until March 31, 1992, for the filing of a plan of compromise or arrangement with its creditors. This short period would be attractive in that it would minimize the risk to the secured creditors. However, having regard to the nature of the business and to the fact that re-financing and the sale of the business have been explored as recently as October 1991, the period suggested is unrealistic.

25 It is perhaps significant that in the interim the applicant seeks the power to "proceed with an orderly liquidation" of the assets, with termination of employment of such of its employees and the termination of such supplier arrangements as is appropriate. The applicant also wishes to have the right to seek offers for the assets in whole or in part.

26 The application is supported by Quebec Equity and CCFL/RICC, and opposed by Paribas, Royal Bank and K Mart. It was argued on behalf of the applicant that Royal Bank need not be considered, because it will be paid out in any event on March 6. It was clear that it would be paid out not by the applicant but by K Mart, which would simply step into the shoes of Royal Bank.

27 The position of Paribas, Royal Bank and K Mart was that default had occurred, the enterprise was losing money, but nobody knew how much, all sides had lost any confidence in management, and they, as the leading secured creditors, would be prejudiced by any delay in the appointing of a receiver.

28 In terms of prejudice, it is significant that K Mart supports the position of Paribas rather than the position of the applicant. It is significant because K Mart has guaranteed the applicant's debt to the Royal Bank and remains as a covenantor on approximately 111 of Bargain Harold's leases. On the other hand, there is at least the possibility that K Mart's position is dictated in part by the fact that, to some extent, it might be regarded as a competitor of Bargain Harold's.

29 Paribas is concerned about its security position in part because the cause of the $20,000,000 loss has yet to be identified with reasonable certainty, and may never be identified. The $20,000,000 figure itself is not certain. Because the management information systems in place appear to be incapable of providing timely and accurate financial information, Bargain Harold's may continue to operate in a significant loss position. As these losses are incurred, they would directly erode the value of Paribas' security. In particular, if supplier, landlord and employee liabilities are kept current by Bargain Harold's, then continuing operating losses would directly and immediately erode the amount and value of the inventories, these being Paribas' primary source of security. On the other hand, if Bargain Harold's defaults in payment of government or employee liabilities, those liabilities may gain priority over Paribas' position as senior secured creditor.

30 In Bargain Harold's business, inventory turns over rapidly. This factor, combined with continuing operating losses, could result in large inventory shrinkages over a very short period of time. In addition, because of the mismanagement of inventory, Paribas is concerned about the quality of inventory that will remain on the shelves as the financial position of the company continues to deteriorate. The more valuable and quickly resalable goods will be turning over rapidly, but the less valuable goods will remain on the shelves.

31 Bargain Harold's launched its C.C.A.A. application first. Its material is replete with admissions of mismanagement. Counsel for Paribas was very critical of the applicant's material and pointed out a number of instances of what he described as non-disclosure. In my view, nothing turns on this point. It can be explained by the shortness of time available to the applicant after the collapse of negotiations and by the fact that the applicant and Paribas, understandably, have two quite different perspectives of the mismanagement.

32 The original material of the applicant had a great deal to say on the subject of mismanagement, but nothing on the question of improving that management. The material of Paribas was then served and, in response, an affidavit of C.R. Middleton, sworn February 26, was delivered. That affidavit states that:

> There will be major changes to existing senior management of Bargain Harold's to be implemented immediately upon granting the relief being sought by Bargain Harold's.

Why the acquisition of new management was conditioned upon the making of a C.C.A.A. order was not explained. There was no identification of the proposed new management, nor any statement from her, him or them, as to plans for the future.

33 The applicant has brought itself within the ambit of the legislation in that it is insolvent, it has outstanding trust debentures, and it seeks to make an arrangement with its creditors, including the holders of those debentures. While the lack of any plan may be surprising in view of the length of the negotiations, it may be that it had no reason to expect the negotiations would not succeed.

34 During the course of the hearing, I raised the question of the onus on an application under the C.C.A.A. As might have been expected, the applicant relied upon the fact that the C.C.A.A. is remedial legislation and is to be given a broad and liberal interpretation. Counsel for Paribas argued that as Bargain Harold's was applying to the court for the exercise of its discretion, the onus was on Bargain Harold's. In *Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 1 C.B.R. (3d) 101, (sub nom. *Elan Corp. v. Comiskey)* 1 O.R. (3d) 289, 41 O.A.C. 282, at pp. 306, 307 [O.R.], Doherty J.A. said:

> Because of that 'broad constituency' the court must, when considering applications brought under the Act, have regard not only to the individuals and organizations directly affected by the application, but also to the wider public interest.

> That interest is generally, but not always, served by permitting an attempt at reorganization: ...

Accepting that approach, the onus is really on Paribas et al. to show why the order should not be granted.

35 The jurisprudence is clear that if it is obvious that no plan will be found acceptable to the required percentages of creditors, then the application should be refused. The fact that Paribas, the Royal Bank and K Mart now say there is no plan that they would approve, does not put an end to the inquiry. All affected constituencies must be considered, including secured, preferred and unsecured creditors, employees, landlords, shareholders, and the public generally: *Icor Oil & Gas Co. v. Canadian Imperial Bank of Commerce* (1989), 102 A.R. 161 (Q.B.), per Marshall J. at p. 164 ¶21.

36 As Doherty J.A. said in *Elan* at p. 317b [O.R.]:

> As I see it, the key to this analysis rests in the measurement of the risk to the Bank inherent in the granting of the s.5 order. If there was a real risk that the loan made by the Bank would become undersecured during the operative period of the s.5 order, I would be inclined to hold that the Bank should not have that risk forced on it by the court.

37 As to the degree of persuasion required, Doherty J.A. in *Elan* said at p.316 [O.R.]:

> I agree that the feasibility of the plan is a relevant and significant factor to be considered in determining whether to order a meeting of creditors: Edwards, 'Re-organizations under the Companies' Creditors Arrangement Act', *supra*, at pp. 594-595. I would not, however, impose a heavy burden on the debtor company to establish the likelihood of ultimate success from the outset. As the Act will often be the last refuge for failing companies, it is to be expected that many of the proposed plans of reorganization will involve variables and contingencies which will make the plan's ultimate acceptability to the creditors and the court very uncertain at the time the initial application is made.

38 *In Ultracare Management Inc. v. Zevenberger (Trustee of)* (1990), 3 C.B.R. (3d) 151, (sub nom. *Ultracare Management Inc. v. Gammon)* 1 O.R. (3d) 321 (Gen. Div.), Hoilett J., at p.330 f [O.R.], suggests that the test is whether the plan, or in the present case, any plan, "has a probable chance of acceptance."

39 These two standards are in conflict, *Ultracare* requiring the probability of success, and *Elan* requiring something less. Having regard to the nature of the legislation, I prefer the test enunciated by Doherty J.A. in *Elan*. In *First Treasury Financial Inc. v. Cango Petroleums Inc.* (1991), 3 C.B.R. (3d) 232 (Ont. Gen. Div.) at p.238, I expressed the view that the statute required "a reasonable chance" that a plan would be accepted.

40 A court must be concerned with the nature of the evidence presented in cases such as this. The applicant's main affidavit was sworn on February 25, Paribas' affidavit on the 26th, and the applicant's in response on the 26th. There has been no opportunity for cross-examination. As a consequence, there is a very heavy responsibility on counsel and the court must be mindful of the frailties of the evidence.

41 Section 6 of the C.C.A.A. requires approval of the plan or arrangement by a majority in number representing

three-fourths in value of the creditors. Where there are different classes of creditors, the section requires a majority in number representing three-fourths in value of the creditors in each class. Having regard to the evidence presented and its shortcomings, I am unable to conclude that there is any reasonable prospect of the applicant being able to devise a plan or arrangement which would meet the approval requirements of s.6 of the Act. Amongst the most important elements in reaching this decision is the fact that the applicant still does not know the precise nature of the problem which brought about its present financial circumstances. According to its own auditors, the cause or causes may never be known. There is also the fact, probably related to this first element, that the applicant has no specific idea how its operation can be salvaged, other than to suggest "downsizing." There is no reason to believe that that downsizing can be done any more efficiently by the applicant than by a receiver.

42 Next is the need to borrow still more money from the Royal Bank in order to continue in business at all. The fact that the Royal Bank may be paid out on March 6 is irrelevant. In order to carry on during the proposed stay period, the applicant requires funds. No source other than the Royal Bank, or in its shoes, K Mart, has been suggested. More to the point, perhaps, no offer has been made by QECC or by CCFL, both of whom are substantial shareholders and both of whom, it was argued, are in a position to assist in refinancing.

43 Another factor is the failed or abandoned attempt to raise $15 million in October 1991. Yet another is the complete loss of confidence in the management of the company. To this is added the failure of the applicant to suggest who the new management might be.

44 The only proposal suggested by way of an alternative to a C.C.A.A. order was the appointment of a receiver and manager. As in *Cango*, there is no reason to believe that if a receiver were appointed, any more unemployment would result than if the present applicant were left in charge.

45 At the conclusion of the hearing of this matter on February 26, I indicated my intention to reserve my decision. Counsel for the applicant indicated that as its financial difficulties were now a matter of public knowledge, some order should be made to protect the company pending my decision. As counsel were unable to agree on anything, I made an interim order under s.11 of the C.C.A.A. and appointed Price Waterhouse monitor for the interim period. That order and monitorship is now terminated.

46 An order will go dismissing the C.C.A.A. application. An order will also go appointing Price Waterhouse as receiver and manager of the applicant, effective immediately. If there is any difficulty in settling the form of order, I may be spoken to. Although the question was not raised during the course of argument, the order should confer upon the receiver the power to make an assignment in bankruptcy should it be so advised. A major asset of Bargain Harold's consists of leases. A trustee in bankruptcy has much wider powers to deal with leases than does a receiver.

47 The matter of the expertise of Price Waterhouse in this area of business was not addressed. It is an area where a great deal of money can be lost in a very short time. If Price Waterhouse does not presently have expertise in this field, it should acquire it forthwith.

48 The draft order which appears at Tab 1 of the receivership motion record deals with the costs of Paribas on that motion. I may be spoken to by letter as to the costs, including quantum, of all parties to the C.C.A.A. application.

Application dismissed.

End of Document

TAB 6

2008 CarswellOnt 4046
Ontario Superior Court of Justice

Caterpillar Financial Services Ltd. v. Hard-Rock Paving Co.

2008 CarswellOnt 4046, 169 A.C.W.S. (3d) 789, 45 C.B.R. (5th) 87

Caterpillar Financial Services Limited v. Hard-Rock Paving Company Limited, Diamond Stonebridge Contracting Inc., Hard-Rock Construction Inc., 942355 Ontario Limited and 942356 Ontario Limited

H.J. Wilton-Siegel J.

Heard: June 10, 2008
Judgment: June 10, 2008
Docket: CV-08-00007504-00CL

Counsel: Steven T. Weisz, Katherine McEachern, Michael McGraw for Applicant, Caterpillar Financial Services Limited
Gary H. Luftspring for GCNA as D & O Insurer
Raymond M. Slattery, David T. Ullmann for Hard-Rock Paving Company Limited
Craig J. Hill for Gaurantee Company of North America
Tim Hogan for BDO Dunwoody
Andrew Hatnay, Demetrios Yiokaris for Labourers International Local 837

Subject: Insolvency; Civil Practice and Procedu

Headnote

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Miscellaneous issues

Substantially all of proceeds of sale of debtors' assets and business would be for benefit of creditor — Debtors brought application for extension of stay of proceedings under Companies' Creditors Arrangement Act and approval of $1 million of additional DIP financing to allow it to complete sales process currently underway — Creditor sought to terminate proceedings under Act with assignment of debtor into bankruptcy — Debtors' application granted — Quantum of probable decline in creditor's security position was neither large amount nor material in context of creditor's overall exposure — Substitution of trustee in bankruptcy or interim receiver to take carriage of sale process would entail considerable additional costs and time that had to be weighed against estimated decline in security that would result if DIP financing was approved — Sale on going-concern basis would yield sales proceeds that were no lower than, and quite possibly higher than, sales proceeds likely to result from sale on liquidation basis — Monitor's opinion was that it would expect current sales process to yield amount in excess of amount likely realizable from sales process conducted by trustee in bankruptcy or interim receiver — Monitor was of opinion that such difference would be at least equal to creditor's security deficiency — Evidence suggested that approval of DIP financing would not adversely affect creditor's security position any more than assignment into bankruptcy, and may well have more positive financial result to creditor.

Table of Authorities

Statutes considered:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

APPLICATION by debtors for extension of stay of proceedings under *Companies' Creditors Arrangement Act* and approval of $1 million of additional DIP financing to allow it to complete sales process currently underway.

***H.J. Wilton-Siegel J.*:**

1 The applicants seek an extension of the stay of proceedings under the CCAA and approval of $1 million of additional DIP financing to be disbursed during June to allow it to complete the sales process currently underway.

2 Caterpillar Financial Services Limited ("CFSL") seeks to terminate the CCAA proceedings with an assignment of the debtor into bankruptcy. As I understand the security held by the secured creditors of the debtors, substantially all of the proceeds of sale of the debtors' assets and business will be for the benefit of CFSL. CFSL envisages continuation of the sales process by the trustee in bankruptcy or an interim receiver appointed by the Court. It has filed a report of KPMG Inc. ("KPMG") that quantifies the net decline in its security position in June if the DIP financing is extended. The amount should be reduced by the amount of interest accruing on the stayed loans and leases, which would be incurred irrespective of whether DIP financing is approved. The net amount is herein referred to as the "CFSL Security Deficiency".

3 I would note that, while CFSL also suggests that the actual decline in its security position could be higher as a result of lower accounts receivable related to possible unidentified trust claims not included in the MOT deduction in the KPMG calculation, this is entirely speculative. There is no evidence of any such claims despite KPMG's involvement.

4 In considering the applicants' requested relief, the Court should have regard to the number of employees who would be affected if the business were shut down and the nature of that impact on the particular community involved. However, by itself, that consideration would not be sufficient to decide the issue if CFSL were able to demonstrate a significant adverse impact on its security position likely to result if the DIP financing were approved.

5 Accordingly, the Court must assess whether, on the evidence before it, it is probable that the current sales process would net higher proceeds than a sale after an assignment into bankruptcy.

6 The quantum of the probable decline in the CFSL security position, as calculated by KPMG, is neither a large amount nor material in the context of CFSL's overall exposure. The substitution of a trustee in bankruptcy or interim receiver to take carriage of the sales process would entail considerable additional costs and time which must be weighed against the estimated decline in security that will result if the DIP financing is approved.

7 In addition, a sale on a going-concern basis will yield sales proceeds that are no lower than, and quite possibly higher than, the sales proceeds likely to result from a sale on a liquidation basis. The Monitor has given its opinion to the Court at the hearing that it would expect the current sales process to yield an amount in excess of the amount likely realizable from a sales process conducted by a trustee in bankruptcy or an interim receiver. The Monitor is of the opinion that such difference would be at least equal to the CFSL Security Deficiency. The Monitor has indicated that it is prepared to put this opinion in writing in a supplemental report to be filed with the Court.

8 Based on the foregoing, while nothing is certain these circumstances, the evidence before the Court suggests that approval of the additional DIP financing will not adversely affect CFSL's security position any more than an assignment into bankruptcy of the applicants, and may well have a more positive financial result to CFSL.

9 Accordingly, the stay of proceedings under the CCAA is extended and DIP financing in an amount not exceeding $1 million is approved, subject to the approval of the Court of a term sheet implementing such DIP financing.

Application granted.

End of Document

TAB 7

Most Negative Treatment: Distinguished
Most Recent Distinguished: Worldspan Marine Inc., Re | 2011 BCSC 1758, 2011 CarswellBC 3667, 86 C.B.R. (5th) 119, [2012] B.C.W.L.D. 2061, 211 A.C.W.S. (3d) 557 | (B.C. S.C., Dec 21, 2011)

2005 ABQB 91
Alberta Court of Queen's Bench

San Francisco Gifts Ltd., Re

2005 CarswellAlta 174, 2005 ABQB 91, [2005] A.W.L.D. 1426, [2005] A.J. No. 131, 10 C.B.R. (5th) 275, 137 A.C.W.S. (3d) 242, 378 A.R. 361, 42 Alta. L.R. (4th) 377

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

And In the Matter of a Plan of Compromise or Arrangement of San Francisco Gifts Ltd., San Francisco Retail Gifts Incorporated (Previously Called San Francisco Gifts Incorporated), San Francisco Gift Stores Limited, San Francisco Gifts (Atlantic) Limited, San Francisco Stores Ltd., San Francisco Gifts & Novelties Inc., San Francisco Gifts & Novelty Merchandising Corporation (Previously Called San Francisco Gifts and Novelty Corporation), San Francisco (The Rock) Ltd. (Previously Called San Francisco Newfoundland Ltd.) And San Francisco Retail Gifts & Novelties Limited (Previously Called San Francisco Gifts & Novelties Limited)

Topolniski J.

Heard: January 17, 2005
Judgment: February 9, 2005
Docket: Edmonton 0403-00170

Counsel: Richard T.G. Reeson, Q.C., John Bridgadear, Howard J. Sniderman for Companies
Michael McCabe, Q.C. for Monitor, Browning Crocker Inc.
Jeremy H. Hockin for Oxford Properties Group Inc., Ivanhoe Cambridge 1 Inc.; 20 Vic Management Ltd.; Morguard Investments Ltd.; Morguard Real Estate Investments Trust; Millwoods Town Centre, Edmonton; Park Place, Lethbridge; Metro Town, Burnaby, B.C.; Northgate Mall, Edmonton; Brandon Shopping Mall, MB; Herongate Mall, Ottawa; Westmount Shopping Centre, London; Village Mall, St. John's NFLD; Kingsway Garden Mall; Westbrook Mall; Bonnie Doon Shopping Centre; Red Deer Centre; Marlborough Mall; Circile Park Mall; Kildonan Place Mall; Cambridge Centre; Oshawa Centre; Tecumseh Mall; Downtown Chatham Centre; Simcoe Town Centre; Niagara Square; Halifax Shopping Centre; RioCan Property Services; 1113443 Ontario Inc.; Shoppers World, Brampton, ON; Tillicum Mall, Victoria, BC; Confederation Mall, Saskatoon, SK; Parkland Mall, Yorkton, SK; Cambrian Mall, Sault Ste. Marie, ON; Northumberland Mall, Cobourg, ON; Orangeville Mall, Orangeville, ON; Renfrew Mall, Renfrew, ON; Orillia Square Mall, Orillia, ON; Elgin Mall, St. Thomas, ON; Lawrence Square, North York, ON; Trinity Conception Square, Carbonear, NFLD; Charlottetown Mall, Charlottetown PEI; Timiskaming Square
Kent Rowan for Locher Evers International, Neuvo Rags, Quality Press
Tim Shelley (Agent Employee) for Lauer Transportation Services

Subject: Insolvency; Civil Practice and Procedure

Headnote

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Arrangements — Effect of arrangement — Stay of proceedings

Debtor operated national chain of novelty goods stores with some 400 employees — Debtor obtained Companies' Creditors Arrangement Act (CCAA) protection on January 7, 2000 — Stay of proceedings under CCAA was extended three times with expectation that entire CCAA process would be completed by February 7th, 2005 — On December 30, 2004, debtor pleaded guilty to nine counts of wilful copyright infringement and paid $150,000 fine — Debtor had sold lamps with counterfeit safety certification labels and was found to have other counterfeit goods in its possession — Debtor brought application for further extension of time — Application granted — Stay was extended to July 19, 2005 — This was not case where debtor's business practices were so offensive as to warrant refusal of extension on public policy grounds — Debtor's conduct was illegal and offensive, but debtor had already been condemned for its illegal conduct in appropriate forum — Denying extension would be additional form of punishment — Of greater concern was effect on unsecured creditors who would be denied right to vote on plan and any chance for small financial recovery — Debtor met prerequisites of acting with due diligence and in good faith in working towards presenting plan of arrangement to its creditors — Delay was primarily attributable to time required for debtor to seek leave to appeal from prior classification decision — Monitor was satisfied that debtor was financially viable despite payment of fine — Potential adverse effect of debtor's misconduct on business relationships was sheer speculation at this point.

Table of Authorities

Cases considered by *Topolniski J.*:

Agro Pacific Industries Ltd., Re (2000), 2000 BCSC 837, 2000 CarswellBC 1143, 76 B.C.L.R. (3d) 364, 5 B.L.R. (3d) 203 (B.C. S.C.) — considered

Associated Investors of Canada Ltd., Re (1987), 56 Alta. L.R. (2d) 259, [1988] 2 W.W.R. 211, 38 B.L.R. 148, 67 C.B.R. (N.S.) 237, (sub nom. *First Investors Corp., Re)* 46 D.L.R. (4th) 669, 1987 CarswellAlta 330 (Alta. Q.B.) — considered

Associated Investors of Canada Ltd., Re (1988), 60 Alta. L.R. (2d) 242, 89 A.R. 344, 71 C.B.R. (N.S.) 71, 1988 CarswellAlta 310 (Alta. C.A.) — considered

Avery Construction Co., Re (1942), [1942] 4 D.L.R. 558, 24 C.B.R. 17, 1942 CarswellOnt 86 (Ont. S.C.) — referred to

Canadian Cottons Ltd., Re (1951), 33 C.B.R. 38, [1952] Que. S.C. 276, 1951 CarswellQue 27 (Que. S.C.) — referred to

Fracmaster Ltd., Re (1999), 1999 CarswellAlta 461, 245 A.R. 102, 11 C.B.R. (4th) 204 (Alta. Q.B.) — referred to

Hongkong Bank of Canada v. Chef Ready Foods Ltd. (1990), 51 B.C.L.R. (2d) 84, 4 C.B.R. (3d) 311, (sub nom. *Chef Ready Foods Ltd. v. Hongkong Bank of Canada)* [1991] 2 W.W.R. 136, 1990 CarswellBC 394 (B.C. C.A.) — referred to

Juniper Lumber Co., Re (2000), 2000 CarswellNB 117 (N.B. Q.B.) — considered

Juniper Lumber Co., Re (2001), 2001 NBCA 30, 2001 CarswellNB 114 (N.B. C.A.) — referred to

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

Nova Metal Products Inc. v. Comiskey (Trustee of) (1990), 1 C.B.R. (3d) 101, (sub nom. *Elan Corp. v. Comiskey)* 1 O.R. (3d) 289, (sub nom. *Elan Corp. v. Comiskey)* 41 O.A.C. 282, 1990 CarswellOnt 139 (Ont. C.A.) — referred to

Pacific National Lease Holding Corp., Re (August 17, 1992), Doc. A922870 (B.C. S.C.) — referred to

Pacific National Lease Holding Corp., Re (1992), 72 B.C.L.R. (2d) 368, 19 B.C.A.C. 134, 34 W.A.C. 134, 15 C.B.R. (3d) 265, 1992 CarswellBC 524 (B.C. C.A. [In Chambers]) — referred to

Rio Nevada Energy Inc., Re (2000), 2000 CarswellAlta 1584, 283 A.R. 146 (Alta. Q.B.) — considered

Royal Bank v. Fracmaster Ltd. (1999), 1999 CarswellAlta 539, (sub nom. *UTI Energy Corp. v. Fracmaster Ltd.)* 244 A.R. 93, (sub nom. *UTI Energy Corp. v. Fracmaster Ltd.)* 209 W.A.C. 93, 11 C.B.R. (4th) 230 (Alta. C.A.) — referred to

Sairex GmbH v. Prudential Steel Ltd. (1991), 8 C.B.R. (3d) 62, 1991 CarswellOnt 215 (Ont. Gen. Div.) — considered

Skeena Cellulose Inc., Re (2001), 2001 BCSC 1423, 2001 CarswellBC 2226, 29 C.B.R. (4th) 157 (B.C. S.C.) — considered

Statutes considered:

Bankruptcy Code, 11 U.S.C. 1982
Chapter 11 — referred to

Business Corporations Act, R.S.A. 2000, c. B-9
Generally — referred to

Companies Act, 1929 (19 & 20 Geo. 5), c. 23
s. 153 — referred to

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

s. 11(6) — referred to

Copyright Act, R.S.C. 1985, c. C-42
Generally — referred to

s. 42 — referred to

APPLICATION by debtor for further extension of stay of proceedings under *Companies' Creditors Arrangement Act.*

***Topolniski J.*:**

Introduction

1 The San Francisco group of companies (San Francisco) obtained *Companies' Creditors Arrangement Act*[1] (*CCAA*) protection on January 7, 2000 (Initial Order). Key to that protection was the requisite stay of proceedings that gives a debtor company breathing room to formulate a plan of arrangement. The stay was extended three times thereafter with the expectation that the entire *CCAA* process would be completed by February 7th, 2005. That date was not met. Accordingly, San Francisco now applies to have the stay extended to June 30, 2005.

2 A small group of landlords opposes the motion on the basis of San Francisco's recent guilty plea to *Copyright Act* offenses and the sentencing judge's description of San Francisco's conduct as: "...a despicable fraud on the public. Not only not insignificant but bordering on a massive scale..." The landlords suggest that this precludes any possibility of the company having acted in "good faith" and therefore having met the statutory prerequisite to an extension. Further, they contend that extending the stay would bring the administration of justice into disrepute.

3 San Francisco acknowledges that its conduct was stupid, offensive and dangerous. That said, it contends that it already has been sanctioned and that it has "paid its debt to society." It argues that subjecting it to another consequence in this proceeding would be akin to double jeopardy. Apart from the obvious consequential harm to the company itself, San Francisco expresses concern that its creditors might be disadvantaged if it is forced into bankruptcy.

4 While there has been some delay in moving this matter forward towards the creditor vote, this delay is primarily attributable to the time it took San Francisco to deal with leave to appeal my classification decision of September 28, 2004. Despite the opposing landlords' mild protestations to the contrary, it is evident that the company has acted with due diligence. The real focus of this application is on the meaning and scope of the term "good faith" as that term is used in s. 11(6) of the *CCAA*, and on whether San Francisco's conduct renders it unworthy of the protective umbrella of the Act in its restructuring efforts. It also raises questions about the role of a supervising court in *CCAA* proceedings.

Background

5 San Francisco operates a national chain of novelty goods stores from its head office in Edmonton, Alberta. It currently has 62 locations and approximately 400 employees.

6 The group of companies is comprised of the operating company, San Francisco Gifts Ltd., and a number of hollow nominee companies. The operating company holds all of the group's assets. It is 100 percent owned by Laurier Investments Corp., which in turn is 100 percent owned by Barry Slawsky (Slawsky), the driving force behind the companies.

7 Apart from typical priority challenges in insolvency matters, this proceeding has been punctuated by a series of challenges to the process and its continuation, led primarily by a group of landlords that includes the opposing landlords.

8 On December 30, 2004, San Francisco pleaded guilty to nine charges under s. 42 of the *Copyright Act*,[2] which creates offences for a variety of conduct constituting wilful copyright infringement. The evidence in that proceeding established that:

> (a) An investigation by the St. John's, Newfoundland, Fire Marshall, arising from a complaint about a faulty lamp sold by San Francisco, led to the discovery that the lamp bore a counterfeit safety certification label commonly called a "UL" label.[3] The R.C.M.P. conducted searches of San Francisco stores across the country, its head office, and a warehouse, which turned up other counterfeit electrical UL labels as well as counterfeit products bearing the symbols of trademark holders of Playboy, Marvel Comics and others.
>
> (b) Counterfeit UL labels were found in the offices of Slawsky and San Francisco's Head of Sales. There was also a fax from "a Chinese location" found in Slawsky's office that threatened that a report to Canadian authorities about the counterfeit safety labels would be made if payment was not forthcoming.
>
> (c) *Copyright Act* charges against Slawsky were withdrawn when San Francisco entered a plea of guilty to the charges;
>
> (d) The sentencing judge accepted counsels' joint submission that a $150,000.00 fine would be appropriate. In passing sentence, he condemned the company's conduct, particularly as it related to the counterfeit labels, expressing grave concern for the safety of unknowing consumers.[4]
>
> (e) San Francisco was co-operative during the R.C.M.P. investigation and the Crown's prosecution of the case.
>
> (f) San Francisco had been convicted of similar offences in 1998.

9 Judge Stevens-Guille's condemnation of San Francisco's conduct was the subject of local and national newspaper coverage.

10 The company paid the $150,000.00 fine from last year's profits.

Analysis

Fundamentals

11 The well established remedial purpose of the *CCAA* is to facilitate the making of a compromise or arrangement by an insolvent company with its creditors to the end that the company is able to stay in business. The premise is that this will result in a benefit to the company, its creditors and employees.[5] The Act is to be given a large and liberal interpretation.[6]

12 The court's jurisdiction under s. 11(6) to extend a stay of proceedings (beyond the initial 30 days of a *CCAA* order) is preconditioned on the applicant satisfying it that:

> (a) circumstances exist that make such an order appropriate; and
>
> (b) the applicant has acted, and is acting, in good faith and with due diligence.

13 Whether it is "appropriate" to make the order is not dependant on finding "due diligence" and "good faith." Indeed, refusal on that basis can be the result of an independent or interconnected finding. Stays of proceedings have been refused where the company is hopelessly insolvent; has acted in bad faith;[7] or where the plan of arrangement is unworkable, impractical or essentially doomed to failure.[8]

Meaning of "Good Faith"

14 The term "good faith" is not defined in the *CCAA* and there is a paucity of judicial consideration about its meaning in the context of stay extension applications. The opposing landlords on this application rely on the following definition of "good faith" found in *Black's Law Dictionary* to support the proposition that good faith encompasses general commercial fairness and honesty:

> A state of mind consisting of: (1) honesty in belief or purpose, (2) faithfulness to one's duty or obligation, (3) observance of reasonable commercial standards of fair dealings in a given trade or business, or (4) absence of intent to defraud or seek unconscionable advantage.[9] [Emphasis added]

15 "Good faith" is defined as "honesty of intention" in the *Concise Oxford Dictionary*.[10]

16 Regardless of which definition is used, honesty is at the core. Honesty is what the opposing landlords urge is desperately wanting now and, as evidenced by San Francisco's earlier conviction for *Copyright Act* offences, was wanting in the past.

17 Accepting that the duty of "good faith" requires honesty, the question is whether that duty is owed to the court and the stakeholders directly affected by the process, including investors, creditors and employees, or does the *CCAA* cast a broader net by requiring good faith in terms of the company's dealings with the public at large? As will be seen from the following review of the jurisprudence, it usually means the former.

18 *Rio Nevada Energy Inc., Re*[11] and *Skeena Cellulose Inc., Re*[12] both involved opposed stay extension applications. In *Skeena Cellulose Inc.*, one of the company's two major secured creditors argued that the company's failure to carry out certain layoffs in the time recommended by the monitor showed a lack of good faith and due diligence. Brenner C.J.S.C. found that the delay in carrying out the layoffs was not a matter of bad faith. Given the severe consequences of terminating the stay, he granted the extension.

19 Romaine J. rejected a suggestion of lack of good faith arising from a creditor dispute and allegations of debtor dishonesty in *Rio Nevada Energy Inc.*, finding that: "Rio Nevada has acted and is acting in good faith *with respect to these proceedings*."[13] [Emphasis added]

20 *Sairex GmbH v. Prudential Steel Ltd.*[14] involved an application by a creditor to proceed against a company under *CCAA* protection. Farley J. declined the application despite his sympathy for the creditor's position and his view that the creditor could make out a fairly strong case. He said: "... I would think that public policy also dictates that a company under *CCAA* protection or about to apply for it should not be allowed to engage in very offensive business practices against another and thumb its nose at the world from the safety of the *CCAA*."[15] In the end, he concluded that the dominant purpose behind

the company's actions was not to harm the creditor.

21 Inventory suppliers in *Agro Pacific Industries Ltd., Re*[16] sought to set aside a *CCAA* stay on the ground that the company had not been acting in good faith in entering into contracts. The suppliers' contention that the company knew it was in shaky financial circumstances when it ordered goods and that it did so to pay down the secured creditors was rejected by Thackeray J. He was not satisfied that there was any lack of good faith or collusion between the company and its secured creditors to disadvantage the unsecured creditors.

22 *Juniper Lumber Co., Re*[17] addressed a creditor's allegations of bad faith in the context of an application to set aside the *ex parte* Initial Order. Turnbull J. held that, while fraud may not always preclude *CCAA* relief, it was of such a magnitude in that case as to warrant setting aside the order. He commented that: "basic honesty has to be present" in the course of conduct between a bank and its customer.[18] However, his decision was overturned by the Court of Appeal because the necessary evidentiary foundation was wanting.[19]

23 *Nova Metal Products Inc. v. Comiskey (Trustee of)*,[20] although addressing instant trust deeds, which are no longer of concern under the present *CCAA*, offers a useful discussion of "good faith." Doherty J.A., dissenting in part, commented:

> ...A debtor company should not be allowed to use the Act for any purpose other than to attempt a legitimate reorganization. If the purpose of the application is to advantage one creditor over another, to defeat the legitimate interests of creditors, to delay the inevitable failure of the debtor company, or for some other improper purpose, the court has the means available to it, apart entirely from s. 3 of the Act, to prevent misuse of the Act. In cases where the debtor company acts in bad faith, the court may refuse to order a meeting of creditors, it may deny interim protection, it may vary interim protection initially given when the bad faith is shown, or it may refuse to sanction any plan which emanates from the meeting of the creditors.[21]

24 Doherty J.A. referred to an article by L. Crozier, "*Good Faith and the Companies' Creditors Arrangement Act*,"[22] in which the author contends that the possibility of abuse and manipulation by debtors should be checked by implying a requirement of good faith, as American bankruptcy courts routinely do by invoking good faith to dismiss applications under Chapter 11 of the *Bankruptcy Code* where the debtor's conduct in filing for reorganization is found to constitute bad faith.[23] He also suggests that, as a result of the injunctive nature of the stay, the court's power to take into account the debtor's conduct is inherent in its equitable jurisdiction.

25 An obligation of good faith in the context of an application to sanction a plan of arrangement was implied in *Associated Investors of Canada Ltd., Re*[24] While *First Investors* was an atypical *CCAA* proceeding, it is worth discussion. Allegations that fraud had been committed on creditors and consumers/investors led to the additional appointment of both a receiver and an inspector under the Alberta *Business Corporations Act*. The inspector had a broad mandate to investigate the company's affairs and business practices that included inquiring into whether the company had intended to defraud anyone.

26 Berger J. (as he then was) noted that the *CCAA* is derived from s. 153 of the English *Companies Act*, 1929 (19 and 20 Geo. 5) c. 23. Having sought assistance from other legislation with wording similar to the *CCAA* and with a genesis in the British statute,[25] he concluded that the court should not sanction an illegal, improper or unfair plan of arrangement.[26] He emphasized that: "If evidence of fraud, negligence, wrongdoing or illegality emerges, the Court may be called upon by interested parties to draw certain conclusions in fact and in law that bear directly upon the Plans of Arrangement."[27] He also determined that, while it might be expedient to approve the plans, the court was bound to proceed with caution, "so as to ensure that wrongful acts, if any, do not receive judicial sanction."[28]

27 In the end, Berger J. adjourned the application pending receipt of a report by the inspector. His decision was reversed on appeal[29] on the basis that there was nothing in the plans that sanctioned wrongful acts or omissions. The Court of Appeal remitted the matter back for reconsideration on the merits, stating that while the discretion to be exercised must relate to the merits or propriety of the plans, the court could consider whether approving the plans would sanction possible wrongdoing or otherwise hinder later litigation.

Supervising Court's Role

28 The court's role during the stay period has been described as a supervisory one, meant to: "...preserve the *status quo* and to move the process along to the point where an arrangement or compromise is approved or it is evident that the attempt is doomed to failure."[30] That is not to say that the supervising judge is limited to a myopic view of balance sheets, scheduling of creditors' meetings and the like. On the contrary, this role requires attention to changing circumstances and vigilance in ensuring that a delicate balance of interests is maintained.

29 Although the supervising judge's main concern centres on actions affecting stakeholders in the proceeding, she is also responsible for protecting the institutional integrity of the *CCAA* courts, preserving their public esteem, and doing equity.[31] She cannot turn a blind eye to corporate conduct that could affect the public's confidence in the *CCAA* process but must be alive to concerns of offensive business practices that are of such gravity that the interests of stakeholders in the proceeding must yield to those of the public at large.

Conclusions

30 While "good faith" in the context of stay applications is generally focused on the debtor's dealings with stakeholders, concern for the broader public interest mandates that a stay not be granted if the result will be to condone wrongdoing.[32]

31 Although there is a possibility that a debtor company's business practices will be so offensive as to warrant refusal of a stay extension on public policy grounds, this is not such a case. Clearly, San Francisco's sale of knockoff goods was illegal and offensive. Most troubling was its sale to an unwitting public of goods bearing counterfeit safety labels. Allowing the stay to continue in this case is not to minimize the repugnant nature of San Francisco's conduct. However, the company has been condemned for its illegal conduct in the appropriate forum and punishment levied. Denying the stay extension application would be an additional form of punishment. Of greater concern is the effect that it would have on San Francisco's creditors, particularly the unsecured creditors, who would be denied their right to vote on the plan and whatever chance they might have for a small financial recovery, one which they, for the most part, patiently await.

32 San Francisco has met the prerequisites that it has acted and is acting with due diligence and in good faith in working towards presenting a plan of arrangement to its creditors. Appreciating that the *CCAA* is to be given a broad and liberal interpretation to give effect to its remedial purpose, I am satisfied that, in the circumstances, extending the stay of proceedings is appropriate. The stay is extended to July 19, 2005. The revised time frame for next steps in the proceedings is set out on the attached Schedule.

33 Although San Francisco has paid the $150,000.00 fine, the Monitor is satisfied that the company's current cash flow statements indicate that it is financially viable. Whether San Francisco can weather any loss of public confidence arising from its actions and resulting conviction is yet to be seen. Its creditors may look more critically at the plan of arrangement, and its

customers and business associates may reconsider the value of their continued relationship with the company. However, that is sheer speculation.

Schedule

Time Frames

1. February 14, 2005 Date Monitor posts Notice to Creditors on website
2. February 14, 2005 Date Monitor publishes the advertisement for one day in Globe & Mail or National Post
3. April 1, 2005 Date for receipt of claims from creditors
4. May 13, 2005 Date by which Monitor must send Notice of Revision or Disallowance.
5. June 13, 2005 Last date for bringing application to challenge a Notice of Revision or Disallowance.
6. June 27, 2005 Date for creditors meeting to vote on the Plan.
7. July 11, 2005 Date for court application to approve Plan (if required).
8. August 18, 2005 Date for Distribution to Prove Unsecured Claims

Stay Extended to July 19, 2005

Application granted.

Footnotes

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

[2] R.S.C. 1985, c. C-42.

[3] Underwriters' Laboratories (UL) operates facilities globally for the testing, certification and quality assessment of products, systems and services. Products are tested to Canadian standards and, if the product complies with those standards, UL issues an identification or listing mark confirming certification (Transcript of the proceedings held December 30, 2004 at pp.4-5)

[4] Judge Stevens-Guille said: "Quite frankly, this is and should be described as nothing else than a despicable fraud on the public. Not only not insignificant but bordering on a massive scale company, stores, all of these places that we have been told they had stores...We are talking about electrical appliances that cause fires bought by someone who whether they relied on the UL certificate or not it had a certificate on it and to go to the exercise of getting cheap stuff somewhere and dressing it up with false labels and false safety certificates causes me great pause, such pause that if it were an individual who pled guilty before me today my starting point would be a term of imprisonment in a federal penitentiary, without a doubt." (Transcript of the proceedings held December 30, 2004 at pp. 18/15-18 and 19/2-11).

[5] See for example *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 4 C.B.R. (3d) 311 (B.C. C.A.) and *Meridian Development Inc. v. Toronto Dominion Bank* (1984), 52 C.B.R. (N.S.) 109 (Alta. Q.B.).

[6] *Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 1 C.B.R. (3d) 101 (Ont. C.A.).

[7] *Avery Construction Co., Re*, [1942] 4 D.L.R. 558 (Ont. S.C.), at 559.

[8] *Fracmaster Ltd., Re* (1999), 11 C.B.R. (4th) 204 (Alta. Q.B.); aff'd (1999), 11 C.B.R. (4th) 230 (Alta. C.A.).

9 *Black's Law Dictionary*, 7th ed. (St. Paul, Minnesota: West Group, 1999), p.701.

10 *The Concise Oxford Dictionary of Current English*, 6th ed., (Oxford, Eng.: Clarendon Press, 1976), p.373.

11 (2000), 283 A.R. 146 (Alta. Q.B.).

12 2001 BCSC 1423, 29 C.B.R. (4th) 157 (B.C. S.C.).

13 *Rio Nevada Energy Inc.*, at para. 31.

14 (1991), 8 C.B.R. (3d) 62 (Ont. Gen. Div.).

15 *Sairex GmbH*, at p. 73.

16 2000 BCSC 837, 76 B.C.L.R. (3d) 364 (B.C. S.C.).

17 *Juniper Lumber Co., Re* (N.B. Q.B.).

18 *Juniper Lumber Co., Re*, at para. 13.

19 2001 NBCA 30 (N.B. C.A.).

20 (1990), 1 O.R. (3d) 289 (Ont. C.A.).

21 *Elan Corp.*, at p. 313.

22 (1989), 15 Can. Bus. L.J. 89.

23 Crozier cites *Victory Construction Co. Inc., Re*, 9 B.R. 549 as an example of this. The court in that case found that the debtor company's purpose in filing under c. 11 was to isolate assets from its creditors rather than to reorganize the business. At p. 558, the court commented that good faith was "an iinplicit prerequisite to the filing or continuation of a proceeding under Chapter 11 of the *Code*."

24 (1987), 46 D.L.R. (4th) 669 (Alta. Q.B.), at 673-674, (1987), 67 C.B.R. (N.S.) 237 (Alta. Q.B.); See also *Agro Pacific Industries Ltd., Re*, footnote 16, at para. 40 where Thackray J. held that there was an implied duty of good faith on initial applications.

25 *First Investors*, at p. 676.

26 *First Investors*, at p. 677.

27 *First Investors*, at p. 678.

28 *First Investors*, at p. 678.

29 (1988), 89 A.R. 344, 71 C.B.R. (N.S.) 71 (Alta. C.A.).

30 McFarlane J.A. in *Pacific National Lease Holding Corp., Re* (1992), 15 C.B.R. (3d) 265 (B.C. C.A. [In Chambers]), at 270, quoting with approval Brenner J. in the court below at (B.C. S.C.) at para. 26.

31 L. J. Crozier, footnote 22 at p. 95, quotes Edith H. Jones, in "The Good Faith Requirement in Bankruptcy," Proceedings of the 61st Annual Meeting of the National Conference of Bankruptcy Judges, 1987, as statingd that: "... the bankruptcy judge usually at the instance of counsel, upon the filing of appropriate motions, is principally responsible to protect the institutional integrity of the

bankruptcy courts, preserve their public esteem, and do equity in specific cases."

32 *Associated Investors of Canada Ltd., Re* (1988), 89 A.R. 344 (Alta. C.A.) at para. 16; *Canadian Cottons Ltd., Re* (1951), 33 C.B.R. 38 (Que. S.C.).

End of Document

TAB 8

COURT FILE NO.: 03-CL-005013
DATE: 20030707

ONTARIO

SUPERIOR COURT OF JUSTICE

RE: SLMsoft INC. – CCAA APPLICATION)
)
ORAL REASONS GIVEN: JUNE 27, 2003)

GROUND J.

[1] Although I have some concerns about certain past activities of the Applicant, I am satisfied that, with respect to this CCAA application, the Applicant has acted and is acting in good faith and with due diligence. Substantial progress has been made in downsizing the Applicant, a business plan has been developed, certain accounts receivable have been collected, arrangements have been made for DIP financing, an analysis of outstanding contracts has been undertaken to determine their viability, new contracts for developed software are being negotiated, the Applicant has recently achieved a slight profitability and most post-filing obligations have been paid.

[2] As to the other arm of the test that "circumstances exist that make such an order appropriate", that is a more difficult call. Whether or not Insight has a blocking position, I am not overly impressed by the position recently taken by Insight that it will not support any restructuring plan put forward by the Applicant. This seems to me to be an irrational position to take and I have on many occasions seen an opposed creditor change its position when a plan is introduced. I am also not satisfied that Insight, which appears to be the only opposed creditor, will be unduly jeopardized or prejudiced if an extension is granted. The prejudice to Insight is, in my view, the same as the prejudice to any other creditor in a CCAA situation in that DIP financing and other priority charges will rank ahead of it and the value of the Applicant may decrease during the stay period if a plan is not ultimately approved.

[3] As to the position of the Applicant, whether the test to be applied is that there is no prospect of success, that the plan is doomed to failure, or that there is no reasonable possibility of success, I think it is premature to make that determination. It is also significant, in my view, that the Monitor feels strongly that there is a realistic possibility of a successful restructuring, and the Independent Monitor has not taken a position in that regard. Accordingly, as indicated, I am prepared to extend the stay to August 8, 2003 on terms that any motion for a further extension will be brought before me during the week of August 5, 2003, and that during the extension period, the Applicant, with the assistance of the monitor, will:

(a) comply with the information requests of Richter as set out in its first report;

(b) provide to Insight and Richter a listing of accounts receivable with aging information and estimates as to collectability;

(c) comply with its obligations to pay installments of arrears to CCRA;

(d) complete arrangements for the advance of the full $1,000,000.00 DIP facility;

(e) provide Insight and Richter with revised cash flows for the period through to July 31, 2003;

(f) ensure that during that period, no compensation is paid by the Applicant to Ms. Molly Misir;

(g) make no termination payments pursuant to the employment contracts referred to in paragraph 8.3 of the Richter report and negotiate the removal from such contracts of the termination payments now provided for;

(h) continue with efforts to negotiate a satisfactory arrangement for performance guarantees, which will be acceptable to the Applicant's customers, and which will provide that any access to source codes to be granted to third parties pursuant to such arrangements will be subject to the approval of this court; and

(i) resolve with Insight the issue of the conversion of the convertible debenture into equity or bring a motion before this court for the determination of that issue.

[4] The Monitor is to review the functions fulfilled and the compensation paid to Misir family members by the Applicant.

[5] Any information provided to Richter and Insight with respect to the financial position, customers and contracts of the Applicant is to be treated as confidential.

[6] Order to issue accordingly.

Ground J.

Released: July 07, 2003

COURT FILE NO.: 03-CL-005013
DATE: 20030707

ONTARIO

SUPERIOR COURT OF JUSTICE

RE: SLMsoft INC. – CCAA APPLICATION

ORAL REASONS

Ground J.

Released: July 07, 2003

TAB 9

2011 NSSC 306
Nova Scotia Supreme Court

Scanwood Canada Ltd., Re

2011 CarswellNS 562, 2011 NSSC 306, 305 N.S.R. (2d) 30, 84 C.B.R. (5th) 51, 966 A.P.R. 30

In the Matter of: The Companies' Creditors Arrangement Act, 1985, c. C-36, as amended

In the Matter of: A Plan of Compromise or Arrangement of Scanwood Canada Limited, a body corporate under the laws of the Province of Nova Scotia

Suzanne M. Hood J.

Heard: April 18, 2011
Oral reasons: April 18, 2011
Written reasons: July 27, 2011
Docket: Hfx. 342377

Counsel: D. Bruce Clarke, Q.C. for Appellant
Thomas Boyne, Q.C. for Royal Bank of Canada
Stephen Kingston, Q.C., Joe McNally for Business Development Bank of Canada
Gavin MacDonald for Green Hunt Wedlake
Tim Hill for Uniboard Canada Inc.
Brian Stilwell, Thomas Khattar (AC) for IKEA
Joseph Pettigrew, Sheldon Shoo for Province of Nova Scotia
Susan Taylor for ACOA

Subject: Insolvency

Headnote

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Initial application — Grant of stay — Extension of order

Debtor company was granted protection of Companies' Creditors Arrangement Act (CCAA) — Debtor applied for further extension of CCAA protection, and submitted new manufacturing model at hearing — Application dismissed — Request for extension denied — Further extension of thirty days was not appropriate in circumstances — Debtor had been acting in good faith and with due diligence — Onus was on debtor to establish that extension was appropriate in circumstances — Recent revised manufacturing model was too late to establish that, within 30 days, there could be plan of arrangement — Monitor had no opportunity to consider new manufacturing model — New manufacturing model was so recent that there was no indication of its ability to attract equity investors — Monitor reviewed debtor's financial position and prospects, and did not support extension.

Table of Authorities

Cases considered by *Suzanne M. Hood J.*:

Federal Gypsum Co., Re (2007), 2007 NSSC 347, 2007 CarswellNS 629, 261 N.S.R. (2d) 299, 40 C.B.R. (5th) 80, 835 A.P.R. 299 (N.S. S.C.) — considered

Hunters Trailer & Marine Ltd., Re (2000), 2000 ABQB 952, 2000 CarswellAlta 1776, 5 C.B.R. (5th) 64 (Alta. Q.B.) — considered

Inducon Development Corp., Re (1991), 8 C.B.R. (3d) 306, 1991 CarswellOnt 219 (Ont. Gen. Div.) — considered

Starcom International Optics Corp., Re (1998), 1998 CarswellBC 477, 3 C.B.R. (4th) 177 (B.C. S.C. [In Chambers]) — considered

Statutes considered:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

s. 11.02(2) [en. 2005, c. 47, s. 128] — considered

s. 11.02(3) [en. 2005, c. 47, s. 128] — considered

s. 23(1)(k) — referred to

s. 36(1) — referred to

APPLICATION by debtor company for further extension of *Companies' Creditors Arrangement Act* protection.

***Suzanne M. Hood J.*:**

1 Scanwood seeks a further extension of the CCAA protection. It is supported in this application by Uniboard, an unsecured creditor. IKEA does not oppose the extension. The Province of Nova Scotia and the Federal Government take no position on it. It is opposed by BDC and RBC. The Monitor, in his fifth report dated April 15, says on page 11:

> Despite our belief that Scanwood has been acting in good faith and with due diligence, unless further evidence to support an extension of the Stay of Proceedings is presented and appropriately justified, it is the Monitor's opinion that the extension requested is not appropriate in these circumstances.

2 Since the date of that report, an Eighth Affidavit has been filed by Mr. Thorn. He attaches to it a revised manufacturing model which he says will "increase productivity and profitability." It says it "will allow Scanwood to attract equity investment which will then allow us to return to the development of a viable Plan of Arrangement."

3 He says in para. 10:

> Ikea has expressed great interest in our re-development plan and has advised me that it does not oppose our extension application.

4 The Monitor says that he has not had sufficient opportunity to review this model and can offer no comments on it. He reiterates his position taken in the fifth report that he does not support an extension.

5 Scanwood says there are three options available to me today: 1) I can grant the extension; 2) I can grant the extension and give additional powers to the Monitor pursuant to s. 23(1) (k) and s. 36(1) of the *Act* or 3) I could grant the receivership which has been proposed by BDC, which application I note has not yet been heard.

6 The *Act* provides in s. 11.02(2) that I may grant an extension. Section 11.02(3) provides that:

> 11.0.2(3) the court shall not make the order unless:
>
> (a) the applicant satisfies the court that circumstances exist that make the order appropriate; and
>
> b) in the case of an order under subsection (2), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

7 No one has expressed any concern with respect to item b) and no one has said that that has not been satisfied. I conclude that the applicant has acted and is acting in good faith and with due diligence.

8 The real question for me is whether the order is appropriate. BDC and RBC say it is not. They refer to decisions where "appropriate circumstances" have been considered.

9 In *Starcom International Optics Corp., Re*, [1998] B.C.J. No. 506 (B.C. S.C. [In Chambers])], the court said an important consideration is whether the attempt to restructure is "doomed to failure." (para. 23) In *Federal Gypsum Co., Re*, 2007 NSSC 347 (N.S. S.C.), the same phrase was used. In *Hunters Trailer & Marine Ltd., Re*, 2000 ABQB 952 (Alta. Q.B.), Wachowich, A.C.J.Q.B. said in para. 18:

> 18. A stay of proceedings should not be granted under the *CCAA* where it would only prolong the inevitable, or where the position of the objecting respondents would be unduly jeopardized: ... The B.C. Court of Appeal said that CCAA orders should only be made if there is a reasonable prospect of a successful restructuring. ... Given my conclusion that further DIP financing should not be permitted, it is clear that Hunters will be unable to finance its operating costs, and therefore the business is doomed to failure. But even if DIP financing continued, the problems with cashflow, discussed above, suggest that Hunters has no reasonable prospect of becoming viable again.

10 Both Mr. Kingston and Mr. Boyne referred to Mr. Thorn's Seventh Affidavit. They say that a restructuring is doomed to fail and that granting an extension would merely prolong the inevitable. The factors to which they refer are (paraphrasing from Mr. Thorn's Affidavit): that Scanwood has acknowledged it not longer believes it is possible for it to file a viable Plan of Arrangement; its own draft projections indicate that it could at best produce a seven percent rate of return prior to principal repayments and dividends to unsecured creditors; that BDC has lost confidence in Scanwood; that the RBC requires Scanwood's operating line of credit be paid out; that Scanwood would be obliged to find a new operating lender; that IKEA has refused to waive its setoff; that IKEA's sales of products such as those Scanwood manufactures is showing a decreasing trend; that IDEA is Scanwood's sole customer and it has refused to allow its Supply Agreement with Scanwood to be assigned to a new owner or new control group; and that Scanwood had asked its employees to agreed to certain concessions and the request was overwhelmingly rejected; the Federal Government proposes to apply to seek to have GST credits go to the payment of CRA and ACOA debt; Scanwood's attempts to sell its assets to a third party failed; a substantial equity investment is required and the problems with respect to that are set out in Mr. Thorn's Affidavit at para. 23.

> 23. Scanwood has spoken with several potential equity investors in an attempt to create a viable Plan. We have not been able to find anyone willing to invest in Scanwood because:
>
> (a) Scanwood may not have a term lender if BDC wishes to be paid out;
>
> (b) Scanwood must pay out the RBC line of credit;
>
> (c) Scanwood can not readily arrange for a replacement operating lender due to IKEA's right of set-off unless the IKEA loan can be paid out in full;
>
> (d) Projections do not reliably support sufficient cash flows back to investors after payment of operating costs, principal debt repayment and CCAA dividend payments;
>
> (e) Our employees are not prepared to make any concessions that would assist us in achieving reliable profitability.

11 Boyne's written submissions as well refer to that Affidavit. He also expressed concern about the jeopardy to creditors, including his client, RBC, of a further extension devaluing its security.

12 Scanwood says that Option No. 2 is the best option. It would allow Scanwood the opportunity to find investors willing to invest based upon the model attached to the Eighth Affidavit. At the same time, if additional powers are granted to the Monitor, it would allow the Monitor to have the same powers as a receiver. If no plan was then forthcoming, the work done by the Monitor with expanded powers would be useful in a receivership.

13 Mr. Hill for Uniboard says this option does not merely delay the inevitable. He points out that the purpose of the *Act* is to allow for the rehabilitation of companies in financial distress. He says there is potential with the revised business plan for equity investment. He says the position of creditors is not jeopardized because the assets are still there, the building and equipment, and no additional financing is being requested.

14 Mr. Clarke for Scanwood says the court should be careful not to take the liquidated values as fair market values. He says there is still $20 million in assets.

15 The onus is on Scanwood to satisfy me that the extension is appropriate in the circumstances. A new manufacturing

model has been put before the court this morning. The Monitor has not had an opportunity to consider it. It is so recent that there is no indication of its ability to attract equity investors. BDC has characterized it as a "last gasp" referring to the decision cited by Mr. Boyne *Inducon Development Corp., Re* (1991), 8 C.B.R. (3d) 306 (Ont. Gen. Div.) where the court said the CCAA:

> ... is not, however, designed to be preventative. CCAA should not be the last gasp of a dying company; it should be implemented, if it is to be implemented, at a stage prior to the death throe.

16 Of particular importance to me is the position of the Monitor. The Monitor is independent not only of Scanwood but also of the creditors. His position should carry some considerable weight with the court. The Monitor has reviewed the company's financial position and prospects. In this case, the Monitor does not support the extension. That in itself does not mean I must do as the Monitor says, but it is a factor in determining if an extension is appropriate and whether Scanwood has satisfied me that it is so.

17 I have reviewed the Affidavits of Mr. Thorn and, in particular, the Seventh and Eighth Supplemental Affidavits. I conclude that a further extension of thirty days is not appropriate in the circumstances. The circumstances of Scanwood are set out in the Seventh Affidavit, which I have paraphrased above. The need for additional DIP financing in early May is a factor in this conclusion. It is not now being sought but, in Mr. Thorn's Seventh Affidavit, he says in para. 37:

> 37. Scanwood can remain operational on a reduced basis for at least 2 weeks without further DIP financing.

18 In my view, the recent revised manufacturing model is too late to satisfy me that, within 30 days, there could be a plan of arrangement. Having so concluded, it is not necessary for me to consider Option 2 which includes greater powers to a Monitor. I do, however, have some reservations about the applicability of that section to be used as proposed.

19 The request for an extension of CCAA protections is denied.

Application dismissed.

End of Document

TAB 10

2003 ABQB 1015
Alberta Court of Queen's Bench

843504 Alberta Ltd., Re

2003 CarswellAlta 1786, 2003 ABQB 1015, [2003] A.J. No. 1549, 127 A.C.W.S. (3d) 1135, 30 Alta. L.R. (4th) 91, 351 A.R. 222, 4 C.B.R. (5th) 306

In the Matter of the Bankruptcy and Insolvency Act R.S.C. 1985, C. B-3, As Amended and 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 843504 Alberta Ltd. (formerly known as Skyreach Equipment Ltd.)

Topolniski J.

Heard: November 10, 2003
Judgment: December 9, 2003
Docket: Edmonton 0303-19663

Counsel: A. Robert Anderson for EdgeStone Capital Mezzanine Fund II Nominee Inc.
Emi R. Bossio for Ingersoll-Rand Canada Inc.
Michael McCabe for Proposal Trustee, PricewaterhouseCoopers LLP
Kent Rowan for GE Commercial Distribution Finance Canada Inc.
Michael Penny, Stuart Weatherill for Unknown Purchaser
Darren Bieganek for Transportation Lease Systems Inc.
David Stratton for CNH Canada Ltd. (New Holland Construction), New Holland (Canada) Credit Company
Jerry Hockin for JLG Industries Ltd., CAFO Inc.
Rick Reeson for Alberta Treasury Branches

Subject: Insolvency; Corporate and Commercial; Civil Practice and Procedure

Headnote

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Arrangements — Effect of arrangement — Stay of proceedings

Company operated under threat of enforcement proceedings by two of its secured creditors, G Inc. and E Ltd. — Company made arrangement with E Ltd. to seek protection under Companies' Creditors Arrangement Act (CCAA) — Company then filed notice of intention to make proposal under Bankruptcy and Insolvency Act — E Ltd. applied for stay of proceedings under CCAA — Company was placed under protection of CCAA for 30 days and Monitor was appointed — E Ltd. and Monitor brought application to extend stay of proceedings — Application granted — Monitor's proposed restructuring process and timeline contemplated sale of company's assets before plan was developed and presented to creditors — Monitor's proposed process was unacceptable — Monitor acted diligently by moving process towards development of plan — No evidence existed that E Ltd. had acted in bad faith — Monitor had clearly acted in good faith — Extension would provide Monitor with more opportunity to formulate plan to creditors — Controls could be put in place to prevent some creditors from manoeuvring for better position — Further assessment of diligence and good faith could be made at end of extension period — Conditions were imposed on extension of stay of proceedings.

Table of Authorities

Cases considered by *Topolniski J.*:

Alberta (Human Rights Commission) v. Alberta Blue Cross Plan (1983), [1983] 6 W.W.R. 758, 4 C.H.R.R. D/1661, 48 A.R. 192, 1 D.L.R. (4th) 301, 4 Admin. L.R. 135, 84 C.L.L.C. 17,002, 28 Alta. L.R. (2d) 1, 1983 CarswellAlta 159 (Alta. C.A.) — referred to

Allen v. Alberta (2001), 2001 CarswellAlta 1070, [2001] 9 W.W.R. 609, 2001 ABCA 171, 286 A.R. 132, 253 W.A.C. 132, 93 Alta. L.R. (3d) 213 (Alta. C.A.) — referred to

Anvil Range Mining Corp., Re (2001), 2001 CarswellOnt 1325, 25 C.B.R. (4th) 1 (Ont. S.C.J. [Commercial List]) — referred to

Anvil Range Mining Corp., Re (2002), 2002 CarswellOnt 2254, 34 C.B.R. (4th) 157 (Ont. C.A.) — referred to

Blue Range Resource Corp., Re (1999), 1999 CarswellAlta 597, 245 A.R. 154 (Alta. Q.B.) — considered

Campeau Corp., Re (1992), 10 C.B.R. (3d) 104, 1992 CarswellOnt 161 (Ont. Gen. Div.) — referred to

Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re (1998), 72 O.T.C. 99, 1998 CarswellOnt 3346, 5 C.B.R. (4th) 299 (Ont. Gen. Div. [Commercial List]) — considered

Consumers Packaging Inc., Re (2001), 2001 CarswellOnt 3482, 27 C.B.R. (4th) 197, 150 O.A.C. 384, 12 C.P.C. (5th) 208 (Ont. C.A.) — considered

Hovsepian v. Westfair Foods Ltd. (2003), 37 B.L.R. (3d) 78, 2003 ABQB 641, 2003 CarswellAlta 1300 (Alta. Q.B.) — referred to

Lehndorff General Partner Ltd., Re (1993), 17 C.B.R. (3d) 24, 9 B.L.R. (2d) 275, 1993 CarswellOnt 183 (Ont. Gen. Div. [Commercial List]) — referred to

Liberty Oil & Gas Ltd., Re (2002), 2002 ABQB 949, 2002 CarswellAlta 1364, 38 C.B.R. (4th) 227 (Alta. Q.B.) — referred to

Mine Jeffrey inc., Re (2003), 2003 CarswellQue 90, 35 C.C.P.B. 71, [2003] R.J.D.T. 23, 40 C.B.R. (4th) 95, (sub nom. *Syndicat national de l'amiante d'Asbestos c. Mine Jeffrey inc.)* [2003] R.J.Q. 420 (Que. C.A.) — referred to

Olympia & York Developments Ltd., Re (1995), 34 C.B.R. (3d) 93, 1995 CarswellOnt 340 (Ont. Gen. Div. [Commercial List]) — referred to

PSINET Ltd., Re (2001), 2001 CarswellOnt 3405, 28 C.B.R. (4th) 95 (Ont. S.C.J. [Commercial List]) — referred to

Rio Nevada Energy Inc., Re (2000), 2000 CarswellAlta 1584, 283 A.R. 146 (Alta. Q.B.) — referred to

Royal Bank v. Fracmaster Ltd. (1999), 1999 CarswellAlta 539, (sub nom. *UTI Energy Corp. v. Fracmaster Ltd.)* 244 A.R. 93, (sub nom. *UTI Energy Corp. v. Fracmaster Ltd.)* 209 W.A.C. 93, 11 C.B.R. (4th) 230 (Alta. C.A.) — referred to

Sammi Atlas Inc., Re (1998), 1998 CarswellOnt 1145, 3 C.B.R. (4th) 171 (Ont. Gen. Div. [Commercial List]) — referred to

United Used Auto & Truck Parts Ltd., Re (2000), 2000 BCCA 146, 2000 CarswellBC 414, 73 B.C.L.R. (3d) 236, [2000] 5 W.W.R. 178, 16 C.B.R. (4th) 141, 135 B.C.A.C. 96, 221 W.A.C. 96 (B.C. C.A.) — referred to

Statutes considered:

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

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — pursuant to

s. 11(6) — considered

s. 11.7(3) [en. 1997, c. 12, s. 124] — referred to

s. 11.8 [en. 1997, c. 12, s. 124] — referred to

APPLICATION by creditor and monitor to extend stay of proceedings under *Companies' Creditors Arrangement Act.*

Topolniski J. (orally):

Introduction

1 EdgeStone Capital Mezzanine Fund II Ltd., (EdgeStone) a creditor of 84305 Alberta LTD., more commonly known as Skyreach Equipment, and the Monitor of Skyreach, appointed under an Initial Order pursuant to the *Companies Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (CCAA), seek an extension of the stay of proceedings. With the exception of GE Commercial Distribution Finance Canada Inc. (GE), Skyreach's other creditors oppose the extension of the stay. These reasons further expand upon my oral decision on the reasons given on November 10, 2003.

Facts

2 Skyreach Equipment, is a well-known name in Alberta. The company specializes in renting, servicing and selling industrial lifts and aerial work platforms to a variety of business sectors. The Skyreach name, up until a short time ago, graced the arena that is home to the Edmonton Oilers, and continues to be the name of another arena, home to the Kelowna Rockets. It has 142 employees, and operates 12 branches — 19 in Alberta and 3 in British Columbia.

3 Since this spring Skyreach has operated under the threat of enforcement proceedings by its two general secured creditors, G.E. and EdgeStone. It tried to negotiate a going concern sale.

4 On September 19 2003, days after making an arrangement with EdgeStone to seek protection under the CCAA, Skyreach filed a Notice of Intention to make a proposal to its creditors under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 as amended (BIA). EdgeStone then chose to apply instead for the CCAA stay of proceedings, and after a contested motion on October 9, 2003, Skyreach was placed under the protective umbrella of the CCAA for 30 days (Initial Order). PriceWaterhouseCoopers was appointed Monitor, with power to operate the business.

5 EdgeStone and the Monitor apply to have the stay extended. The PIMSI and mortgage creditors oppose the extension application. It is common ground that the onus in applications of this nature is on the applicant to satisfy the test in section 11(6) of the CCAA that:

> a) circumstances exist to make the extension order appropriate and
>
> b) the applicant is acting in good faith and diligently.

The test is not whether the plan of arrangement is doomed to failure — That is the test for terminating, not extending, a stay of proceedings (*Rio Nevada Energy Inc., Re* (2000), 283 A.R. 146 (Alta. Q.B.)).

6 The PIMSI and mortgage creditors argue that EdgeStone has not discharged the onus, asserting that the proceeding has been, and continues to be, an impermissible receivership under the guise of a CCAA restructuring. Further, they object to the Monitor's application on the basis that it is inappropriate for it to take a position in opposition to one of the parties.

7 EdgeStone and the Monitor rely on the Monitor's *Third Report to the Court* and an excerpt from an *Information Circular*. as the necessary evidence of good faith and due diligence in pursuing a plan of arrangement. EdgeStone's officer's affidavit says that, based upon his review of the Monitor's reports, the Monitor is acting diligently, in good faith, and that circumstances exist to warrant the extension.

1. The Initial Order

8 On October 9th, EdgeStone applied to vacate the Notice of Intention and to obtain a CCAA stay of proceedings. GE supported the application. Skyreach took no position. A number of creditors holding PIMSI and mortgage security opposed the initial application on the ground that the CCAA process would benefit only EdgeStone, and therefore was really a receivership for EdgeStone's benefit at the expense of others and an abuse of the CCAA.

9 Appreciating the PIMSI creditors' concerns, I granted the Initial Order with conditions designed to protect the interests of all stakeholders. It provided for the usual 30-day moratorium to permit the development of, at least, a germ of a plan of arrangement, and further required court approval of any sale of assets for more than $100,000 and, in the case of assets subject to PIMSI's, $20,000. It gave the power to carry on business and to solicit invitations from prospective purchasers to the Monitor, and created an expedited process for proving claims for creditors holding PIMSI and mortgage security.

10 The CCAA contemplates a monitor having powers beyond those required to fulfil the traditional role of monitoring the debtor's business and financial affairs and preparing reports for creditors and the court. Section 11.7(3) of the CCAA leaves discretion in the court to authorize functions other then those specifically enumerated by Parliament. Further support for this proposition is the explicit recognition of a monitor carrying on the debtor's business in section 11.8. (*Mine Jeffrey inc., Re* (2003), 40 C.B.R. (4th) 95, [2003] R.J.Q. 420 (Que. C.A.)). The Monitor's ability to carry on business, at least during the Initial Order phase, was considered necessary given the undisputed evidence of corporate interference and allegations of conflict of interest by Skyreach's Director and CEO, and the imminent resignation of the debtor's directors.

2. Subsequent Motions

11 The minutes of the initial order were settled. In the course of that hearing the Monitor's powers were reviewed to ensure that it had the powers necessary to carry on the business and to establish a process for soliciting offers to purchase assets. The intention was to provide sufficient, but not overreaching powers, given the unusual situation of the Monitor, rather than the company, operating the business.

12 GE also sought an order amending an earlier order granted by another judge which permitted funding for Skyreach by GE on specific terms. Notice had not been given to most other creditors. The amending order was refused, with the ability to reapply on notice to affected parties.

3. This Application

13 The CCAA is intended to provide a structured, court supervised environment for the negotiation of compromises between a debtor and its creditors for the benefit of not only those parties, but also other stakeholders such as employees and shareholders. At the end of day, the objective is to enable the debtor to continue in business so that all stakeholders benefit (*United Used Auto & Truck Parts Ltd., Re* (2000), 135 B.C.A.C. 96, 2000 BCCA 146 (B.C. C.A.), at paras. 10 and 11). The CCAA is to be interpreted in a broad and liberal fashion to facilitate that objective. That broad and liberal interpretation, however, must not permit the enhancement of one stakeholders position at the expense of others — there should be no confiscation of legal rights. This requires a balancing of interests, rights and prejudices to "see if rights are compromised . . . and have the pain of the compromise equitably shared." (*Sammi Atlas Inc., Re*, [1998] O.J. No. 1089 (Ont. Gen. Div. [Commercial List]) citing *Campeau Corp., Re*, [1992] O.J. No. 237, 10 C.B.R. (3d) 104 (Ont. Gen. Div.), at 109).

14 As acknowledged by LoVecchio J. in *Blue Range Resources Corp.* (1999), 245 A.R. 154, 1999 ABQB 1038 (Alta. Q.B.), reorganization of a company's affairs under the CCAA may take many forms. There is no one solution that will apply for every company. Solutions may vary from organizational and management restructuring, downsizing, refinancing, or debt to equity conversion — the solutions are generally limited only by the creativity of those structuring the plan of arrangement. That said, the solutions in Alberta generally expect the corporate entity to continue in some form or another and do not allow for a liquidation proposal unless exceptional circumstances exist to justify it, notwithstanding that the CCAA seems to allow it (*Royal Bank v. Fracmaster Ltd.* (1999), 244 A.R. 93, 11 C.B.R. (4th) 230 (Alta. C.A.)). Simply put, in this province the corporate entity is expected to continue in some form or another unless there are exceptional circumstances. Liquidation proceedings are typically reserved for receiverships, windings up or bankruptcy.

15 This is quite different than in Ontario where apparently debtors can use the benefits of the legislation when there is no prospect of corporate survival or no plan of arrangement is proposed: *Anvil Range Mining Corp.* (2002), 25 C.B.R. (4th) 1 (Ont. S.C.J. [Commercial List]), aff'd (2002), 34 C.B.R. (4th) 157 (Ont. C.A.); *Lehndorff General Partner Ltd., Re* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]) at p. 32; *Olympia & York Developments Ltd., Re* (1995), 34 C.B.R. (3d) 93 (Ont. Gen. Div. [Commercial List]) at p. 104; *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (1998), 5 C.B.R. (4th) 299 (Ont. Gen. Div. [Commercial List]) at para. 46.

EdgeStone's Application and Evidence

16 As noted previously, EdgeStone's affidavit is based upon the deponent's review of the Monitor's reports and merely asserts that the Monitor is acting diligently and in good faith, and that circumstances exist to warrant the extension. This offers nothing more than a conclusion about the very determinations that the court is required to make in deciding whether the test has been satisfied. It is of very little assistance, and this form of conclusory affidavit is not acceptable: *Alberta (Human Rights Commission) v. Alberta Blue Cross Plan* (1983), 48 A.R. 192 (Alta. C.A.) at para. 8; *Allen v. Alberta*, [2001] A.J. No. 863, 2001 ABCA 171 (Alta. C.A.) at para. 8; *Hovsepian v. Westfair Foods Ltd.*, [2003] A.J. No. 1133, 2003 ABQB 641 (Alta. Q.B.). I note that the Monitor's report is filed with the court for information purposes and is available to me.

17 GE supports EdgeStone's application, acknowledging that it expects to be paid out in full through an asset sale, and that it continues to be paid full interest at a rate of $15,000 per day on its loan under the terms of a funding order granted earlier by another judge.

The Monitor's Duties, Application, and Evidence

18 The appropriateness of the Monitor's application to extend the stay of proceedings was questioned on the basis that by its actions, the Monitor was favouring the debtor and EdgeStone.

19 As an officer of the court, the Monitor owes a duty to treat all creditors reasonably and fairly. Like a court-appointed receiver or liquidator, its duties are those of a fiduciary.

20 Because of the special circumstances that existed at the date of the Initial Hearing, the Monitor was given the power to carry on Skyreach's business. With that power comes a risk, be it perceived or real, of conflict of interest, and where the Monitor advocates a position or a plan of arrangement that risk may be exacerbated. In making its application for the extension the Monitor presumed that it was reasonable for it to do so since it was operating the business and there were no directors in place. Although motivated by good intentions this gave rise to a perception of conflict of interest, something that must be jealously guarded against. The appointment of a Chief Restructuring Officer or the appointment of new or returning directors can easily avoid perceptions of bias.

21 The Monitor relies on an affidavit that attaches its Third Report to the Court and two pages from an Information Circular. The report indicates that since the Initial Order, the Monitor has taken control of the business, working closely with management. The report indicates that the Monitor has identified excess equipment and undertaken an extensive process to solicit offers for:

a) all or part of the debtor's assets business and undertakings,

b) refinancing,

c) acquisition of the shares of Skyreach (subject to the approval of EdgeStone which holds and may exercise the shares under its security), or

d) any combination thereof.

22 The Monitor has advertised in newspapers, posted information on its national electronic bulletin board and web site, delivered some 300 Information Circulars to prospective purchasers, and set up a data room. Negotiations have begun with prospective purchasers, one of whom has expressed an interest in buying Skyreach's significant tax losses. Counsel for the Monitor, EdgeStone, and GE argued that only a sale of the tax losses will result in some payment to the unsecured creditors at the end of the day. Whether this is likely given voting structures under the CCAA is, of course, yet to be seen.

The proposed restructuring process

23 The Monitor proposes the following restructuring process and time line. The Monitor will:

1. will solicit offers until November 28;

2. report the results of the solicitations to the Court by December 19

3. close transactions after obtaining court approval by January 30 2004, and

4. finally, formulate a plan of arrangement for presentation to the creditors by February 28, 2004.

24 Clearly, this process contemplates the sale of Skyreach's assets, either hard assets or shares, well before a plan is developed and presented to the creditors.

25 The Monitor, EdgeStone and GE urge that this process will maximize recoveries for the stakeholders, contending that the marketplace can best determine value of the debtor's assets. EdgeStone relies on *Consumers Packaging Inc., Re* (2001), 150 O.A.C. 384, 27 C.B.R. (4th) 197 (Ont. C.A.) and *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (1998), 72 O.T.C. 99, 5 C.B.R. (4th) 299 (Ont. Gen. Div. [Commercial List]) in support of the proposition that this is an acceptable practice.

26 Once again, the opposing creditors say that this is simply more evidence that this proceeding is nothing more than a receivership in disguise for EdgeStone's benefit.

27 In *Consumers Packaging Inc.* the court approved a going concern sale before the plan of arrangement was presented because the sale would preserve the business, albeit under new ownership, and because of uncertainty over whether the debtor could continue operations given its financiers' demands.

28 In *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge* provincial and territorial governments decided to transfer responsibility for the Canadian blood supply to a new national agency. The court held that the CCAA was flexible enough that it could be interpreted to convert the company's assets into a cash fund, crystalizing the highest value recovery pool possible. This was advantageous to unsecured creditors, but did not affect creditors with security interests. The Court ruled that it had jurisdiction to grant the order, noting that the proper question was whether the process was appropriate in all of the circumstances.

29 I accept that the need for flexibility in CCAA proceedings may, in the appropriate circumstances, warrant a sale of a significant portion of a debtors assets or undertaking before a plan of arrangement is put to the creditors. (*PSINET Ltd., Re* (2001), 28 C.B.R. (4th) 95 (Ont. S.C.J. [Commercial List]); [2001] O.J. 3829, *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge* and *Consumer's Packaging*). Obviously, each case must be assessed on its own unique facts, but in this case there is no evidence that it is either necessary or in the stakeholders' best interests. Accordingly, at this stage the proposed process is unacceptable. In deciding this, I make no finding as to EdgeStone's *bona fides* nor rule out the prospect of evidence being adduced to establish that it would be appropriate.

30 EdgeStone argues that there is Alberta authority for the sale of all or substantially all of the debtor's assets (*Blue Range Resource Corp, Gauntlet Energy Corp* action 0301-09612, *Liberty Oil & Gas Ltd., Re* action 0201-03299 [2002 CarswellAlta 1364 (Alta. Q.B.)], and *Mirant Canada Energy Marketing Ltd.* action 0301-11094. *Blue Range* and *Liberty Oil & Gas Ltd.* obtained court sanctioning for liquidation-style plans. *Gauntlet* obtained creditor approval for a liquidation-type plan, but the sanctioning hearing has not yet been held. *Mirant's* creditors have not yet approved a liquidation-style plan, although a plan has been circulated to the creditors.

The Extension should be granted

31 Applying the three arms of the test in s. 11.7, I find that the Monitor has acted diligently in moving the process along towards the development of a plan. The fact that the on the evidence before me, I disagree with the proposed timing for steps in the restructuring to occur does not detract from that.

32 Although suspicions are raised by the opposing creditors' arguments, I cannot find on the materials before me that EdgeStone is acting in bad faith. The Monitor is certainly acting in good faith, but that is not an appropriate ingredient in applying the s. 11.7 test.

33 In considering whether circumstances exist for the extension, the following factors assist the applicant:

1. An extension gives the Monitor a better opportunity to formulate and present a plan to the creditors, meeting the purpose and intent of the legislation;

2. With sufficient controls in place, an extension will prevent creditors from maneuvering for a better position (*Rio Nevada Energy Inc.*, and cases cited at para. 36)

3. There is no evidence about whether the anticipated costs of these proceedings will be similar to costs anticipated

in a receivership. What is known is that Skyreach is expected to suffer a $337,000 deficit by the end of January 2004. PIMSI and mortgage creditors want EdgeStone to pay all of CCAA costs. However, it would be inappropriate to allocate costs now since there is no certainty about what benefits will accrue to any given party. That can be done later.

4. The extension Order is only until December 19th. At that time a further assessment of good faith, due diligence, and the appropriateness of the circumstances can be made.

5. I cannot conclude that a liquidation sale is inevitable or the most likely outcome at this stage of the proceedings. The Monitor is offering shares for sale.

6. The prospect of a tax loss sale may have value for unsecured creditors. A tax loss sale is apparently easier to facilitate in CCAA proceedings than other insolvency proceedings;

Order

1. The stay of proceedings under the CCAA is extended to December 19th

2. The Monitor is to hire and hand over possession and operational control of Skyreach to a Chief Restructuring Officer within 14 days;

3. The Monitor is to fulfil its traditional role of monitoring the debtor's business and financial affairs and preparing reports for creditors and court and play a supportive role in developing the plan and presenting it to the creditors;

4. The proposed sale of all or substantially all of the assets before a plan of arrangement is presented to the creditors is not approved.

5. A further stay extension should be supported by evidence demonstrating significant progress towards a plan of arrangement.

6. If the company is unable to present a viable plan of arrangement before a sale of all or substantially all of the assets, the sale documents should be prepared as though for a receivership sale. However, if the company or another applicant proposes a sale before the presentation of a plan, the appropriate application may be made.

7. Assets subject to PIMSI interests used in the company's daily operations are to be paid for in accordance with the terms of the governing agreement.

8. A cost allocation hearing is to be scheduled to follow an application to sanction the plan of arrangement.

Application granted.

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