Court File No. 31-OR-207893-T

ONTARIO
SUPERIOR COURT OF JUSTICE
IN BANKRUPTCY AND INSOLVENCY

IN THE MATTER OF THE BANKRUPTCY OF

ST. MARYS PAPER CORP.

OF THE CITY OF SAULT STE. MARIE, PROVINCE OF ONTARIO

FACTUM OF INTERNATIONAL FOREST PRODUCTS LLC
(Motion to Lift Stay of Proceedings; Application for Bankruptcy Order)
Returnable May 18, 2012

May 17, 2012

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PART I – OVERVIEW

1. This Factum is filed in support of: (a) the motion by International Forest Products LLC (formerly known as International Forest Products Corporation) ("**IFP**") in the receivership proceedings of St. Marys Paper Corp. ("**SMP**") to lift the stay of proceedings (the "**Stay**"); and (b) the application by IFP for a bankruptcy order in respect of SMP.

A. Motion to Lift the Stay

2. IFP seeks an Order lifting the Stay in respect of SMP pursuant to the Order of the Honourable Mr. Justice Campbell dated December 29, 2011, effective December 30, 2011 (the "**Appointment Order**"), for the purpose of filing an application for a bankruptcy order in respect of SMP (the "**Bankruptcy Application**").

3. Ernst & Young Inc. ("**EY**") in its capacity as court-appointed receiver of SMP (the "**Receiver**") does not oppose the lifting of the Stay and has agreed to act as trustee in bankruptcy if a bankruptcy order is granted.

4. The purpose of the Bankruptcy Application is to invoke the scheme of distribution under the *Bankruptcy and Insolvency Act*[1] (the "**BIA**"), specifically to reverse the priority of statutory claims for outstanding vacation pay and harmonized sales tax ("**HST**").

5. Lifting the Stay to enable IFP to file the Bankruptcy Application is appropriate in the circumstances. The majority of the assets of SMP have been sold, the Receiver is ready to distribute the proceeds and, based on the applicable, well-settled case law, it is legitimate and appropriate to seek a bankruptcy order so that a distribution can be made in accordance with the regime established by the BIA.

B. Application for Bankruptcy Order

6. IFP also seeks an Order adjudging SMP bankrupt and appointing EY as trustee.

7. Granting a bankruptcy order with respect to SMP is appropriate as:

(i) the statutory requirements are satisfied: IFP has an unsecured claim against SMP of at least $1,000 and SMP has committed an act of bankruptcy within the six months preceding the filing of the Bankruptcy Application; and

(ii) there is no sufficient cause not to grant a bankruptcy order.

PART II – THE FACTS

8. The parties have filed an agreed statement of facts for the purposes of this motion. Certain of these agreed facts are set out below along with certain additional facts. Any capitalized terms used but not defined herein have the meaning given in the agreed statement of facts.

9. The Mill was shut down in March 2011. The shut down resulted in a liquidity crisis which led to the appointment of the Receiver. The Mill has not operated since March 2011.

10. The main purpose of the receivership proceedings was to liquidate the assets of SMP. The majority of the assets have been sold.

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[1] *Bankruptcy and Insolvency Act,* R.S.C. 1985, c. B-3 ["**BIA**"].

11. IFP brought the Bankruptcy Application returnable May 8, 2012. Certain of SMP's directors appeared and requested an adjournment (the "**Directors**").

12. There is an outstanding motion by the Receiver in the receivership proceedings to, among other things, distribute approximately $4.22 million to IFP less certain reserves. In particular, the Receiver proposes to reserve certain amounts owing to employees which have priority pursuant to the BIA and the *Wage Earner Protection Program Act*[2] ("**WEPPA**").

13. IFP is an unsecured creditor of SMP in an amount exceeding $1,000.

14. In addition to IFP, SMP is indebted to numerous other creditors, and has ceased to meet its liabilities generally as they become due.

15. SMP is indebted to its employees for unpaid vacation pay. At the time of the Receiver's appointment on December 30, 2011, SMP owed its employees approximately $576,404 in unpaid vacation pay.

16. SMP is indebted to the CRA for unpaid HST. On April 17, 2012, the CRA sent a fax to the Receiver, advising of several outstanding balances owed by SMP to the CRA, including HST in the amount of $1,468,685.20.

PART III – ISSUES

17. The issues on this motion and application are as follows:

(a) Should this Court lift the Stay for the purpose of filing the Bankruptcy Application?

(b) Should this Court grant a bankruptcy order in respect of SMP?

(c) If the bankruptcy order is granted, should this Court order that certain property is held in trust and is excluded from the assets of the bankrupt estate?

[2] *Wage Earner Protection Program Act,* S.C. 2005, c. 47, s. 1.

PART IV - THE LAW AND ARGUMENT

A. Lifting The Stay of Proceedings is Appropriate

18. The Stay imposed by the Appointment Order is explicitly subject to the variance by court order or consent of the Receiver:[3]

> [8] THIS COURT ORDERS that no Proceeding against or in respect of the Debtor or the Property shall be commenced or continued except with the written consent of the Receiver or with leave of this Court and any an all Proceedings currently under way against or in respect of the Debtor or the Property are hereby stayed and suspended pending further Order of this Court.
>
> [9] THIS COURT ORDERS that all rights and remedies against the Debtor, the Receiver, or affecting the Property, are hereby stayed and suspended except with the written consent of the Receiver or leave of this Court...

19. The Stay should be lifted. The assets have been liquidated and the Receiver is in possession of the proceeds of sale which it seeks to distribute. Parliament has provided a comprehensive and exhaustive mechanism under the BIA to control distributions and IFP is entitled to seek to invoke that regime to effect the distribution in this case.[4]

20. Orders lifting stays of proceedings in receivership proceedings to permit the filing of bankruptcy applications have been granted where the explicit purpose of the bankruptcy was to reverse the priority of statutory liens.[5]

21. The Receiver does not oppose the lifting of the Stay and has agreed to act as trustee in bankruptcy if a bankruptcy order is granted.

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[3] Order of the Honourable Mr. Justice Campbell dated December 29, 2011.

[4] *Ted Leroy Trucking [Century Services] Ltd., Re*, 2010 SCC 60 at para. 80 ["***Ted Leroy***"]; *Ivaco Inc., Re*, 2006 CarswellOnt 6292 (Ont. C.A.) at para. 76, leave to appeal to SCC granted, 2007 CarswellOnt 2855 ["***Ivaco***"].

[5] See e.g. *Bank of Nova Scotia v. Huronia Precision Plastics Inc.*, 2009 CarswellOnt 374 (Ont. S.C.J. [Commercial List]) at paras. 19 and 20 ["***Huronia***"]; *699845 Ontario Ltd., Re*, 1997 CarswellOnt 2888 (Ont. Gen. Div.) at paras. 9 and 12.

B. Granting a Bankruptcy Order is Appropriate

I) The Statutory Test For Making a Bankruptcy Order is Satisfied

22. In order to make a bankruptcy order, the court must be satisfied that the requirements of section 43(1) and (2) of the BIA have been proven. Each requirement is clearly satisfied and undisputed in this case.

23. SMP is indebted to IFP in the sum of at least US$7,175,678.[6]

24. SMP has committed an act of bankruptcy within the six months preceding the filing of the Bankruptcy Application in that SMP has ceased to meet its liabilities generally as they become due. In addition to its indebtedness to IFP, SMP is indebted to several other creditors, including its employees and the CRA.[7]

25. With respect to section 43(2) of the BIA, IFP is a secured creditor of SMP and has estimated the value of its security at CDN$7,000,000.[8] The balance of the debt due to IFP after deducting the estimated value of its security far exceeds $1,000.

II) No Sufficient Cause Not To Grant Bankruptcy Order

26. After being satisfied that the facts are established that would justify the making of a bankruptcy order, the court has the discretion to refuse to make the order if there is other sufficient cause that the order should not be made.[9] The onus is on the debtor to show sufficient cause why the bankruptcy order should not be granted. If the debtor fails to meet this onus, the court should ordinarily make the bankruptcy order.[10]

27. The discretion to refuse to make a bankruptcy order under section 43(7) of the BIA is typically exercised in two categories of cases: where the applicant creditor has an ulterior

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[6] Affidavit of Truth of Statements in Application of Daniel J. Moore, sworn May 2, 2012 at para. 1, Application Record of IFP dated May 7, 2012 at Tab 1.

[7] Application for Bankruptcy Order dated May 2, 2012 at para. 4, Application Record of IFP dated May 7, 2012 at Tab 1.

[8] *Ibid* at para. 3.

[9] BIA, s. 43(7).

[10] *C. Tokmakjian Ltd., Re*, 2003 CarswellOnt 4616 (Ont. S.C.J.) at para. 46; *Cappe, Re,* 1993 CarswellOnt 198 (Ont. Gen. Div.) at para. 29; affirmed 1994 CarswellOnt 2604 (Ont. C.A.).

motive in seeking the order or where the order would not serve any meaningful purpose.[11] Where the debtor fails to show that the applicant has an ulterior motive in pursuing the application or fails to show that there is no meaningful purpose served by the bankruptcy, the order ought to be granted.

28. IFP is seeking a bankruptcy order to invoke the scheme of distribution under the BIA, specifically, to reverse the priority of the HST and vacation pay claims.

29. It is settled law that the use of the BIA to alter statutory priorities is a legitimate reason to seek a bankruptcy order.[12]

30. IFP has no ulterior motive in pursuing the Bankruptcy Application. A bankruptcy will alter the priorities of certain claims, which is a meaningful and legitimate purpose to seek a bankruptcy order.

C) There Is No Trust For Outstanding HST or Vacation Pay

31. The governing legislation and caselaw are clear that deemed trusts for HST and vacation pay do not survive bankruptcy.[13] In a series of cases, the Supreme Court of Canada has repeatedly held that a province cannot, by legislating a deemed trust, alter the scheme of priorities under the BIA.[14]

32. As these deemed trusts are not trusts within the meaning of the BIA, in order to establish a valid trust in this context, it must be one that meets the requirements of common law trust principles.

33. In this case, there is no property of SMP that (within a bankruptcy) is subject to a trust relating to HST or vacation pay. In addition, there are no legal grounds to impose a remedial constructive trust for such claims.

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[11] *Ivaco, supra* at para. 37.

[12] *Ted Leroy, supra*; *Ivaco, supra* at para. 76; *Huronia, supra* at para. 19; *Textron Financial Canada Ltd.v. Beta Ltée/Beta Brands Ltd.*, 2007 CarswellOnt 6705 (Ont. S.C.J.) at paras. 46-47 ["***Textron***"].

[13] BIA, s. 67(2); *Excise Tax Act*, R.S.C., 1985, c. E-15 ["**ETA**"] s.222(3); *Ted Leroy, supra*; *Textron, ibid.* at para. 28.

[14] See *Indalex Ltd., Re*, 2011 ONCA 265 at para. 191, leave to appeal to SCC granted, 2011 CarswellOnt 13211 ["***Indalex***"]; E.g. *British Columbia v. Henfrey Samson Belair Ltd.*, 2 S.C.R. 24, 1989 CarswellBC 351.

I) No Express Trust

34. In order to establish that property is subject to a trust, a claimant must prove that a valid trust is in existence on the date of bankruptcy. For a valid trust to exist, an arrangement must have the three certainties: certainty of intent, certainty of subject matter and certainty of object.[15]

35. There must be clear intention to create a trust.[16] There is no evidence that any settlor, be it SMP, the Receiver, IFP, or any other party, intended to create a trust. There is no document or other agreement expressly creating a trust with respect to outstanding HST or vacation pay.

36. For a valid trust, the subject matter must be specified and must be in existence on the date of bankruptcy. The funds that the Receiver currently holds and seeks to distribute are the proceeds of the sale of the Property, which, pursuant to the Sale Approval and Vesting Order, stand in the place and stead of the Purchased Assets. A trust claimant is required to trace such proceeds as the subject matter of its trust; of which there is no evidence.

37. With respect to certainty of object, the persons intended to be beneficiaries must be clearly identified. In this case, there is no certainty as to who the beneficiary or beneficiaries of an alleged trust would be. There is no express trust in favour of the Crown with respect to HST and no express trust in favour of SMP's employees or their union with respect to vacation pay.

38. None of the three certainties are satisfied in this case, hence there is no trust.

II) No Grounds to Impose a Constructive Trust

39. There is also no basis to impose a constructive trust in this case.

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[15] *Ted Leroy, supra* at para. 83.

[16] *Ont. Worldair Ltd. Re,* 1983 CarswellOnt 162 (Ont. S.C.) at para. 12; affirmed 1983 CarswellOnt 217 (Ont. C.A.).

40. The remedial constructive trust remedy may be imposed to prevent unjust enrichment or to right wrongful conduct.[17]

41. Courts have expressed reservations about the availability of this discretionary remedy in the insolvency context, where the interests of third party creditors are affected.[18] A constructive trust is not to be imposed without taking into account the interests of others who may be affected by granting the remedy or where it would upset the distribution scheme in the BIA.[19]

a) There is No Unjust Enrichment

42. The requirements for a constructive trust remedy for unjust enrichment are three-fold: an enrichment, a corresponding deprivation and the absence of any juristic reason for the enrichment.[20]

43. There is no enrichment or corresponding deprivation in this case. There is no transaction, payment or other event that has taken place which enriched one party and correspondingly deprived another.

44. The Receiver has sold SMP's assets and holds the proceeds. A distribution to IFP, SMP's first priority secured creditor, is being sought. As a result of a bankruptcy order, if granted, the Crown's claim for outstanding HST and the employees' claims for vacation pay will rank as unsecured claims in the bankruptcy.

45. If there is found to be an enrichment to IFP, such enrichment is not unjust. SMP is deeply indebted to IFP pursuant to various agreements. IFP is an arm's length creditor with a valid security interest in SMP's property and assets.

46. It is settled law that a contractual debtor-creditor relationship constitutes a juristic reason for an enrichment and that constructive trusts do not apply in such circumstances.[21]

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[17] *Indalex, supra* at para. 202; *White, Re*, 2006 CarswellOnt 6424 (Ont. S.C.J.) at para. 19 ["***White***"].

[18] *Melchior v. Cable Estate*, 2007 BCSC 136, 2007 CarswellBC 164 at paras. 68, 84; *White, ibid.* at paras. 23-24; *Caterpillar Financial Services Ltd. v. 360networks Corp.*, 2007 BCCA 14 at para. 66 ["***Caterpillar***"].

[19] *White, ibid* at para. 24.

[20] *Caterpillar*, *supra* at para. 55.

b) There is No Wrongful Conduct or Breach of Fiduciary Duty

47. As stated above, constructive trusts may also be imposed where property is obtained by a wrongful act, notably where there is a breach of fiduciary duty.

48. The requirements for this type of constructive trust are:

(a) a party must have been under an equitable obligation in relation to the activities giving rise to the assets in its hands;

(b) the assets in its hands must be shown to have resulted from its deemed or actual agency activities in breach of its equitable obligation to another party;

(c) there must be a legitimate reason to seek a proprietary remedy; and

(d) there must not be any factors which would render the imposition of a constructive trust unjust in all of the circumstances of the case.[22]

49. In this case, IFP has not and is not under any equitable obligation in relation to the receivership or the proposed bankruptcy. It is an arm's length secured creditor.

50. In *Indalex*, where this type of constructive trust was imposed by the Ontario Court of Appeal, the debtor was a pension plan administrator, and as such was found to owe a fiduciary duty to the pension plan beneficiaries.

51. The situation in *Indalex* is unique and has no application to the case at bar. This Court has cautioned against extending the holding of *Indalex*, which considered what fiduciary duty a debtor company owes to pensioners in respect of underfunded pension liabilities, to other situations.[23]

52. This test for a constructive trust is not applicable to the Receiver. The Receiver is an independent court officer.

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[21] See e.g. *Re Mosaic Group Inc.*, 2004 CarswellOnt 2254 (Ont. S.C.J.) at para. 39; *Canadian Imperial Bank of Commerce v. Melnitzer (Trustee of)*, 1993 CarswellOnt 251 (Ont. C.J. (Gen. Div.) at paras. 104-114.

[22] *Indalex, supra* at para. 203; *White, supra* at para. 19.

[23] F*irst Leaside Wealth Management Int., Re*, 2012 ONSC 1299 at para. 53; see also *White Birch Paper Holding Co., Re*, 2012 QCCS 1679.

53. A court-appointed receiver has a duty to act in the best interests of all parties with an interest in the assets under its control. While there is a fiduciary element to this duty, this is a duty to <u>all</u> creditors.[24] One creditor cannot call on a receiver to act in that creditor's best interests to the detriment of all other creditors.

54. The Receiver was not under any duty to pay outstanding vacation pay or HST or to segregate amounts for such claims.

55. It has been held that an employer does not have a fiduciary duty to make vacation pay payments or segregate funds for such claims and that a receiver's obligations cannot exceed what the company was obliged to do.[25]

56. In addition, there is nothing in the Appointment Order suggesting that the Receiver had any special duties in respect of HST or vacation pay. IFP would have opposed any special treatment of such claims given that IFP intended to seek a bankruptcy order which would reverse the priority of these claims.

57. For the above reasons, neither IFP nor the Receiver had an equitable or fiduciary obligation in respect of HST or vacation pay claims that would indicate that the imposition of a constructive trust is appropriate in this case.

58. The second factor in the test for this type of constructive trust requires a breach of the obligation owed and that such breach is linked to assets in that party's hands.

59. As neither IFP nor the Receiver had an obligation with respect to these claims, neither could have breached an obligation. There are no facts to support an allegation of wrongful conduct or breach of a duty.

60. The third factor requires that there be a legitimate reason for a party to seek a proprietary remedy. In this case, neither the CRA nor the employees (or their union), who would be the beneficiaries of any trust, have sought this remedy.

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[24] See, e.g. *Turbo Logistics Canada Inc. v. HSBC Bank Canada*, 2009 CarswellOnt 5929 (Ont. S.C.J. [Commercial List]) at para. 13.

[25] *Textron, supra* at para. 33.

61. Instead, the Directors seek a declaration that funds are held in trust for the benefit of the CRA and the benefit of employees of SMP.

62. The Directors have statutory liability for unpaid vacation pay and for unpaid HST.[26] The fact that the Directors may be liable for outstanding vacation pay and HST is not a legitimate reason for them to seek a proprietary remedy. Their potential liability does not and should not affect the scheme of distribution set out in the BIA or the legislation and well-settled case law regarding reversal of the priority of such claims in bankruptcy.

63. The fourth and final requirement, regarding fairness between the parties, was satisfied in *Indalex* because the secured creditor that stood to benefit was related to the party that was found to have breached a duty. Justice Gillese wrote: "This is not a case in which the secured creditor is an arm's length third party..."[27]

64. The facts here are distinguishable. IFP is an arm's length third party secured creditor.

65. In *Indalex*, Justice Gillese also wrote that "the Plans' beneficiaries are not mere unsecured creditors. They are unsecured creditors to whom Indalex owed a fiduciary duty by virtue of its role as the Plans' administrator. There is a significant difference, in my view, between being a mere unsecured creditor and being an unsecured creditor to whom a fiduciary duty is owed."[28]

66. If a bankruptcy order is granted in the case at bar, the employees and the Crown will be unsecured creditors. These creditors were not and are not owed a fiduciary duty.

67. Furthermore, Parliament has taken steps to ensure that employees are protected for amounts owing to them, including with respect to vacation pay. Certain statutory protections for employees are contained in the WEPPA as well as in the BIA.

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[26] *Business Corporations Act*, R.S.O. 1990, c. B. 16, s. 131; *Employment Standards Act 2000*, S.O. 2000, c. 41, s. 81; ETA, s. 323.
[27] *Indalex, supra* at para. 184.
[28] *Indalex, supra* at para. 200.

68. The BIA provides special protection to employees for unpaid wages (including vacation pay) both in receivership and in bankruptcy.[29] As described above, the Receiver has proposed a reserve from the proposed distribution to IFP for such amounts, to the extent applicable to SMP, which IFP does not oppose.

69. The Directors are seeking protection for outstanding vacation pay which is greater than the protections already provided by applicable legislation. There is no legal basis for this. The rights of employees have been protected by legislation to the extent that Parliament has determined is appropriate, and such protections have been and are being respected by the Receiver and IFP in this case.

70. IFP is not seeking to avoid any legislative protections to which other creditors of SMP are entitled. It is simply seeking a bankruptcy order to invoke the distribution scheme under the BIA.

71. Imposing a constructive trust in this case would be unjust to IFP. There has been no wrongful conduct. No fiduciary duty is owed by IFP to other creditors. It is an arm's length secured creditor seeking a bankruptcy order.

PART IV – RELIEF REQUESTED

72. IFP therefore requests that its motion be granted and that the Stay imposed by the Appointment Order in respect of SMP be lifted in order that IFP may file the Bankruptcy Application.

73. IFP further requests that the Bankruptcy Application be granted and that a bankruptcy order be made in respect of SMP.

[29] BIA, sections 81.3 and 81.4 and 136(1)(d)

All of which is respectfully submitted,

Michael McGraw / Jenna Willis
Lawyers for International Forest Products LLC

SCHEDULE "A"

AUTHORITIES REFERRED TO

1. *Ted Leroy Trucking [Century Services] Ltd., Re*, 2010 SCC 60
2. *Ivaco Inc., Re*, 2006 CarswellOnt 6292 (Ont. C.A.), leave to appeal to SCC granted, 2007 CarswellOnt 2855
3. *Bank of Nova Scotia v. Huronia Precision Plastics Inc.*, 2009 CarswellOnt 374 (Ont. S.C.J. [Commercial List])
4. *699845 Ontario Ltd., Re*, 1997 CarswellOnt 2888 (Ont. Gen. Div.)
5. *C. Tokmakjian Ltd., Re*, 2003 CarswellOnt 4616 (Ont. S.C.J.)
6. *Re Cappe*, 1993 CarswellOnt 198 (Ont. Gen. Div.); affirmed 1994 CarswellOnt 2604 (Ont. C.A.)
7. *Textron Financial Canada Ltd.v. Beta Ltée/Beta Brands Ltd.*, 2007 CarswellOnt 6705 (Ont. S.C.J.)
8. *Indalex Ltd., Re*, 2011 ONCA 265, leave to appeal to SCC granted, 2011 CarswellOnt 13211
9. *British Columbia v. Henfrey Samson Belair Ltd.*, 2 S.C.R. 24, 1989 CarswellBC 351
10. *Ont. Worldair Ltd. Re,* 1983 CarswellOnt 162 (Ont. S.C.); affirmed 1983 CarswellOnt 217 (Ont. C.A.)
11. *White, Re*, 2006 CarswellOnt 6424 (Ont. S.C.J.)
12. *Melchior v. Cable Estate*, 2007 BCSC 136, 2007 CarswellBC 164
13. *Caterpillar Financial Services Ltd. v. 360networks Corp.*, 2007 BCCA 14
14. *Re Mosaic Group Inc.* (2004), 3 C.B.R. (5th) 40, 2004 CarswellOnt 2254 (Ont. S.C.J.)
15. *Canadian Imperial Bank of Commerce v. Melnitzer (Trustee of)*, 1993 CarswellOnt 251 (Ont. C.J. (Gen. Div.)
16. F*irst Leaside Wealth Management Int., Re*, 2012 ONSC 1299
17. *White Birch Paper Holding Co., Re*, 2012 QCCS 1679
18. *Turbo Logistics Canada Inc. v. HSBC Bank Canada*, 2009 CarswellOnt 5929 (Ont. S.C.J. [Commercial List])

SCHEDULE "B"

LEGISLATION

<u>*Bankruptcy and Insolvency Act,* R.S.C. 1985, c. B-3</u>

<u>Section 42</u>

Acts of bankruptcy

42. (1) A debtor commits an act of bankruptcy in each of the following cases:

(*a*) if in Canada or elsewhere he makes an assignment of his property to a trustee for the benefit of his creditors generally, whether it is an assignment authorized by this Act or not;

(*b*) if in Canada or elsewhere the debtor makes a fraudulent gift, delivery or transfer of the debtor's property or of any part of it;

(*c*) if in Canada or elsewhere the debtor makes any transfer of the debtor's property or any part of it, or creates any charge on it, that would under this Act be void or, in the Province of Quebec, null as a fraudulent preference;

(*d*) if, with intent to defeat or delay his creditors, he departs out of Canada, or, being out of Canada, remains out of Canada, or departs from his dwelling-house or otherwise absents himself;

(*e*) if the debtor permits any execution or other process issued against the debtor under which any of the debtor's property is seized, levied on or taken in execution to remain unsatisfied until within five days after the time fixed by the executing officer for the sale of the property or for fifteen days after the seizure, levy or taking in execution, or if any of the debtor's property has been sold by the executing officer, or if the execution or other process has been held by the executing officer for a period of fifteen days after written demand for payment without seizure, levy or taking in execution or satisfaction by payment, or if it is returned endorsed to the effect that the executing officer can find no property on which to levy or to seize or take, but if interpleader or opposition proceedings have been instituted with respect to the property seized, the time elapsing between the date at which the proceedings were instituted and the date at which the proceedings are finally disposed of, settled or abandoned shall not be taken into account in calculating the period of fifteen days;

(*f*) if he exhibits to any meeting of his creditors any statement of his assets and liabilities that shows that he is insolvent, or presents or causes to be presented to any such meeting a written admission of his inability to pay his debts;

(*g*) if he assigns, removes, secretes or disposes of or attempts or is about to assign, remove, secrete or dispose of any of his property with intent to defraud, defeat or delay his creditors or any of them;

(*h*) if he gives notice to any of his creditors that he has suspended or that he is about to suspend payment of his debts;

(*i*) if he defaults in any proposal made under this Act; and

(*j*) if he ceases to meet his liabilities generally as they become due.

Unauthorized assignments are void or null

(2) Every assignment of an insolvent debtor's property other than an assignment authorized by this Act, made by an insolvent debtor for the general benefit of their creditors, is void or, in the Province of Quebec, null.

Section 43

Bankruptcy application

43. (1) Subject to this section, one or more creditors may file in court an application for a bankruptcy order against a debtor if it is alleged in the application that

(*a*) the debt or debts owing to the applicant creditor or creditors amount to one thousand dollars; and

(*b*) the debtor has committed an act of bankruptcy within the six months preceding the filing of the application.

If applicant creditor is a secured creditor

(2) If the applicant creditor referred to in subsection (1) is a secured creditor, they shall in their application either state that they are willing to give up their security for the benefit of the creditors, in the event of a bankruptcy order being made against the debtor, or give an estimate of the value of the applicant creditor's security, and in the latter case they may be admitted as an applicant creditor to the extent of the balance of the debt due to them after deducting the value so estimated, in the same manner as if they were an unsecured creditor.

Affidavit

(3) The application shall be verified by affidavit of the applicant or by someone duly authorized on their behalf having personal knowledge of the facts alleged in the application.

Consolidation of applications

(4) If two or more applications are filed against the same debtor or against joint debtors, the court may consolidate the proceedings or any of them on any terms that the court thinks fit.

Place of filing

(5) The application shall be filed in the court having jurisdiction in the judicial district of the locality of the debtor.

Proof of facts, etc.

(6) At the hearing of the application, the court shall require proof of the facts alleged in the application and of the service of the application, and, if satisfied with the proof, may make a bankruptcy order.

Dismissal of application

(7) If the court is not satisfied with the proof of the facts alleged in the application or of the service of the application, or is satisfied by the debtor that the debtor is able to pay their debts, or that for other sufficient cause no order ought to be made, it shall dismiss the application.

Dismissal with respect to some respondents only

(8) If there are more respondents than one to an application, the court may dismiss the application with respect to one or more of them, without prejudice to the effect of the application as against the other or others of them.

Appointment of trustee

(9) On a bankruptcy order being made, the court shall appoint a licensed trustee as trustee of the property of the bankrupt, having regard, as far as the court considers just, to the wishes of the creditors.

Stay of proceedings if facts denied

(10) If the debtor appears at the hearing of the application and denies the truth of the facts alleged in the application, the court may, instead of dismissing the application, stay all proceedings on the application on any terms that it may see fit to impose on the applicant as to costs or on the debtor to prevent alienation of the debtor's property and for any period of time that may be required for trial of the issue relating to the disputed facts.

Stay of proceedings for other reasons

(11) The court may for other sufficient reason make an order staying the proceedings under an application, either altogether or for a limited time, on any terms and subject to any conditions that the court may think just.

Security for costs

(12) Applicants who are resident out of Canada may be ordered to give security for costs to the debtor, and proceedings under the application may be stayed until the security is furnished.

Bankruptcy order on another application

(13) If proceedings on an application have been stayed or have not been prosecuted with due diligence and effect, the court may, if by reason of the delay or for any other cause it is considered just, substitute or add as applicant any other creditor to whom the debtor may be indebted in the amount required by this Act and make a bankruptcy order on the application of the other creditor, and shall, immediately after making the order, dismiss on any terms that it may consider just the application in the stayed or non-prosecuted proceedings.

Withdrawing application

(14) An application shall not be withdrawn without the leave of the court.

Application against one partner

(15) Any creditor whose claim against a partnership is sufficient to entitle the creditor to present a bankruptcy application may present an application against any one or more partners of the firm without including the others.

Court may consolidate proceedings

(16) If a bankruptcy order has been made against one member of a partnership, any other application against a member of the same partnership shall be filed in or transferred to the same court, and the court may give any directions for consolidating the proceedings under the applications that it thinks just.

Continuance of proceedings on death of debtor

(17) If a debtor against whom an application has been filed dies, the proceedings shall, unless the court otherwise orders, be continued as if the debtor were alive.

Section 67

Property of bankrupt

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

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

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

(b.1) goods and services tax credit payments that are made in prescribed circumstances to the bankrupt and that are not property referred to in paragraph (a) or (b);

(b.2) prescribed payments relating to the essential needs of an individual that are made in prescribed circumstances to the bankrupt and that are not property referred to in paragraph (a) or (b); or

(b.3) without restricting the generality of paragraph (b), property in a registered retirement savings plan or a registered retirement income fund, as those expressions are defined in the Income Tax Act, or in any prescribed plan, other than property contributed to any such plan or fund in the 12 months before the date of bankruptcy,

but it shall comprise

(c) all property wherever situated of the bankrupt at the date of the bankruptcy or that may be acquired by or devolve on the bankrupt before their discharge, including any refund owing to the bankrupt under the Income Tax Act in respect of the calendar year — or the fiscal year of the bankrupt if it is different from the calendar year — in which the bankrupt became a bankrupt, except the portion that

(i) is not subject to the operation of this Act, or

(ii) in the case of a bankrupt who is the judgment debtor named in a garnishee summons served on Her Majesty under the Family Orders and Agreements Enforcement Assistance Act, is garnishable money that is payable to the bankrupt and is to be paid under the garnishee summons, and

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

Deemed trusts

(2) Subject to subsection (3), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property

of a bankrupt shall not be regarded as held in trust for Her Majesty for the purpose of paragraph (1)(a) unless it would be so regarded in the absence of that statutory provision.

Exceptions

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

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

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

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

Section 81.3

Security for unpaid wages, etc. — bankruptcy

81.3 (1) The claim of a clerk, servant, travelling salesperson, labourer or worker who is owed wages, salaries, commissions or compensation by a bankrupt for services rendered during the period beginning on the day that is six months before the date of the initial bankruptcy event and ending on the date of the bankruptcy is secured, as of the date of the bankruptcy, to the extent of $2,000 — less any amount paid for those services by the trustee or by a receiver — by security on the bankrupt's current assets on the date of the bankruptcy.

Commissions

(2) For the purposes of subsection (1), commissions payable when goods are shipped, delivered or paid for, if shipped, delivered or paid for during the period referred to in that subsection, are deemed to have been earned in that period.

Security for disbursements

(3) The claim of a travelling salesperson who is owed money by a bankrupt for disbursements properly incurred in and about the bankrupt's business during the period referred to in subsection (1) is secured, as of the date of the bankruptcy, to the extent of $1,000 — less any amount paid for those disbursements by the trustee or by a receiver — by security on the bankrupt's current assets on that date.

Rank of security

(4) A security under this section ranks above every other claim, right, charge or security against the bankrupt's current assets — regardless of when that other claim, right, charge or security arose — except rights under sections 81.1 and 81.2 and amounts referred to in subsection 67(3) that have been deemed to be held in trust.

Liability of trustee

(5) If the trustee disposes of current assets covered by the security, the trustee is liable for the claim of the clerk, servant, travelling salesperson, labourer or worker to the extent of the amount realized on the disposition of the current assets and is subrogated in and to all rights of the clerk, servant, travelling salesperson, labourer or worker in respect of the amounts paid to that person by the trustee.

Claims of officers and directors

(6) No officer or director of the bankrupt is entitled to have a claim secured under this section.

Non-arm's length

(7) A person who, in respect of a transaction, was not dealing at arm's length with the bankrupt is not entitled to have a claim arising from that transaction secured by this section unless, in the opinion of the trustee, having regard to the circumstances — including the remuneration for, the terms and conditions of and the duration, nature and importance of the services rendered — it is reasonable to conclude that they would have entered into a substantially similar transaction if they had been dealing with each other at arm's length.

Proof by delivery

(8) A claim referred to in this section is proved by delivering to the trustee a proof of claim in the prescribed form.

Definitions

(9) The following definitions apply in this section.

"compensation" includes vacation pay but does not include termination or severance pay.

"receiver" means a receiver within the meaning of subsection 243(2) or an interim receiver appointed under subsection 46(1), 47(1) or 47.1(1).

Section 81.4

Security for unpaid wages, etc. — receivership

81.4 (1) The claim of a clerk, servant, travelling salesperson, labourer or worker who is owed wages, salaries, commissions or compensation by a person who is subject to a receivership for services rendered during the six months before the first day on which there was a receiver in relation to the person is secured, as of that day, to the extent of $2,000 — less any amount paid for those services by a receiver or trustee — by security on the person's current assets that are in the possession or under the control of the receiver.

Commissions

(2) For the purposes of subsection (1), commissions payable when goods are shipped, delivered or paid for, if shipped, delivered or paid for during the six-month period referred to in that subsection, are deemed to have been earned in those six months.

Security for disbursements

(3) The claim of a travelling salesperson who is owed money by a person who is subject to a receivership for disbursements properly incurred in and about the person's business during the six months before the first day on which there was a receiver in relation to the person is secured, as of that day, to the extent of $1,000 — less any amount paid for those disbursements by a receiver or trustee — by security on the person's current assets that are in the possession or under the control of the receiver.

Rank of security

(4) A security under this section ranks above every other claim, right, charge or security against the person's current assets — regardless of when that other claim, right, charge or security arose — except rights under sections 81.1 and 81.2.

Liability of receiver

(5) If the receiver takes possession or in any way disposes of current assets covered by the security, the receiver is liable for the claim of the clerk, servant, travelling salesperson, labourer or worker to the extent of the amount realized on the disposition of the current assets

and is subrogated in and to all rights of the clerk, servant, travelling salesperson, labourer or worker in respect of the amounts paid to that person by the receiver.

Claims of officers and directors

(6) No officer or director of the person who is subject to a receivership is entitled to have a claim secured under this section.

Non-arm's length

(7) A person who, in respect of a transaction, was not dealing at arm's length with a person who is subject to a receivership is not entitled to have a claim arising from that transaction secured by this section unless, in the opinion of the receiver, having regard to the circumstances — including the remuneration for, the terms and conditions of and the duration, nature and importance of the services rendered — it is reasonable to conclude that they would have entered into a substantially similar transaction if they had been dealing with each other at arm's length.

Proof by delivery

(8) A claim referred to in this section is proved by delivering to the receiver a proof of claim in the prescribed form.

Definitions

(9) The following definitions apply in this section.

"compensation" includes vacation pay but does not include termination or severance pay.

"person who is subject to a receivership" means a person any of whose property is in the possession or under the control of a receiver.

"receiver" means a receiver within the meaning of subsection 243(2) or an interim receiver appointed under subsection 46(1), 47(1) or 47.1(1).

<u>Section 136</u>

Priority of claims

136. (1) Subject to the rights of secured creditors, the proceeds realized from the property of a bankrupt shall be applied in priority of payment as follows:

(a) in the case of a deceased bankrupt, the reasonable funeral and testamentary expenses incurred by the legal representative or, in the Province of Quebec, the successors or heirs of the deceased bankrupt;

(b) the costs of administration, in the following order,

(i) the expenses and fees of any person acting under a direction made under paragraph 14.03(1)(a),

(ii) the expenses and fees of the trustee, and

(iii) legal costs;

(c) the levy payable under section 147;

(d) the amount of any wages, salaries, commissions, compensation or disbursements referred to in sections 81.3 and 81.4 that was not paid;

(d.01) the amount equal to the difference a secured creditor would have received but for the operation of sections 81.3 and 81.4 and the amount actually received by the secured creditor;

(d.02) the amount equal to the difference a secured creditor would have received but for the operation of sections 81.5 and 81.6 and the amount actually received by the secured creditor;

(d.1) claims in respect of debts or liabilities referred to in paragraph 178(1)(b) or (c), if provable by virtue of subsection 121(4), for periodic amounts accrued in the year before the date of the bankruptcy that are payable, plus any lump sum amount that is payable;

(e) municipal taxes assessed or levied against the bankrupt, within the two years immediately preceding the bankruptcy, that do not constitute a secured claim against the real property or immovables of the bankrupt, but not exceeding the value of the interest or, in the Province of Quebec, the value of the right of the bankrupt in the property in respect of which the taxes were imposed as declared by the trustee;

(f) the lessor for arrears of rent for a period of three months immediately preceding the bankruptcy and accelerated rent for a period not exceeding three months following the bankruptcy if entitled to accelerated rent under the lease, but the total amount so payable shall not exceed the realization from the property on the premises under lease, and any payment made on account of accelerated rent shall be credited against the amount payable by the trustee for occupation rent;

(g) the fees and costs referred to in subsection 70(2) but only to the extent of the realization from the property exigible thereunder;

(h) in the case of a bankrupt who became bankrupt before the prescribed date, all indebtedness of the bankrupt under any Act respecting workers' compensation, under any Act respecting unemployment insurance or under any provision of the Income Tax Act creating an obligation to pay to Her Majesty amounts that have been deducted or withheld, rateably;

(i) claims resulting from injuries to employees of the bankrupt in respect of which the provisions of any Act respecting workers' compensation do not apply, but only to the extent of moneys received from persons guaranteeing the bankrupt against damages resulting from those injuries; and

(j) in the case of a bankrupt who became bankrupt before the prescribed date, claims of the Crown not mentioned in paragraphs (a) to (i), in right of Canada or any province, rateably notwithstanding any statutory preference to the contrary.

Payment as funds available

(2) Subject to the retention of such sums as may be necessary for the costs of administration or otherwise, payment in accordance with subsection (1) shall be made as soon as funds are available for the purpose.

Balance of claim

(3) A creditor whose rights are restricted by this section is entitled to rank as an unsecured creditor for any balance of claim due him.

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

Section 222

Trust for amounts collected

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

Marginal note:Amounts collected before bankruptcy

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

Marginal note:Withdrawal from trust

(2) A person who holds tax or amounts in trust by reason of subsection (1) may withdraw from the aggregate of the moneys so held in trust

(a) the amount of any input tax credit claimed by the person in a return under this Division filed by the person in respect of a reporting period of the person, and

(b) any amount that may be deducted by the person in determining the net tax of the person for a reporting period of the person,

as and when the return under this Division for the reporting period in which the input tax credit is claimed or the deduction is made is filed with the Minister.

Marginal note:Extension of trust

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

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

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

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

Marginal note:Meaning of security interest

(4) For the purposes of subsections (1) and (3), a security interest does not include a prescribed security interest.

Section 323

Liability of directors

323. (1) If a corporation fails to remit an amount of net tax as required under subsection 228(2) or (2.3) or to pay an amount as required under section 230.1 that was paid to, or was applied to the liability of, the corporation as a net tax refund, the directors of the corporation at the time the corporation was required to remit or pay, as the case may be, the amount are jointly and severally, or solidarily, liable, together with the corporation, to pay the amount and any interest on, or penalties relating to, the amount.

Limitations

(2) A director of a corporation is not liable under subsection (1) unless

(*a*) a certificate for the amount of the corporation's liability referred to in that subsection has been registered in the Federal Court under section 316 and execution for that amount has been returned unsatisfied in whole or in part;

(*b*) the corporation has commenced liquidation or dissolution proceedings or has been dissolved and a claim for the amount of the corporation's liability referred to in subsection (1) has been proved within six months after the earlier of the date of commencement of the proceedings and the date of dissolution; or

(*c*) the corporation has made an assignment or a bankruptcy order has been made against it under the *Bankruptcy and Insolvency Act* and a claim for the amount of the corporation's liability referred to in subsection (1) has been proved within six months after the date of the assignment or bankruptcy order.

Diligence

(3) A director of a corporation is not liable for a failure under subsection (1) where the director exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances.

Assessment

(4) The Minister may assess any person for any amount payable by the person under this section and, where the Minister sends a notice of assessment, sections 296 to 311 apply, with such modifications as the circumstances require.

Time limit

(5) An assessment under subsection (4) of any amount payable by a person who is a director of a corporation shall not be made more than two years after the person last ceased to be a director of the corporation.

Amount recoverable

(6) Where execution referred to in paragraph (2)(*a*) has issued, the amount recoverable from a director is the amount remaining unsatisfied after execution.

Preference

(7) Where a director of a corporation pays an amount in respect of a corporation's liability referred to in subsection (1) that is proved in liquidation, dissolution or bankruptcy proceedings, the director is entitled to any preference that Her Majesty in right of Canada would have been entitled to had the amount not been so paid and, where a certificate that relates to the amount has been registered, the director is entitled to an assignment of the certificate to the extent of the director's payment, which assignment the Minister is empowered to make.

Contribution

(8) A director who satisfies a claim under this section is entitled to contribution from the other directors who were liable for the claim.

Business Corporations Act, R.S.O. 1990, c. B. 16

Section 131

Directors' liability to employees for wages

131. (1) The directors of a corporation are jointly and severally liable to the employees of the corporation for all debts not exceeding six months' wages that become payable while they are directors for services performed for the corporation and for the vacation pay accrued while they are directors for not more than twelve months under the *Employment Standards Act*, and the regulations thereunder, or under any collective agreement made by the corporation. R.S.O. 1990, c. B.16, s. 131 (1).

Limitation of liability

(2) A director is liable under subsection (1) only if,

(a) the corporation is sued in the action against the director and execution against the corporation is returned unsatisfied in whole or in part; or

(b) before or after the action is commenced, the corporation goes into liquidation, is ordered to be wound up or makes an authorized assignment under the *Bankruptcy and Insolvency Act* (Canada), or a receiving order under that Act is made against it, and, in any such case, the claim for the debt has been proved. 2002, c. 24, Sched. B, s. 27 (1).

Idem

(3) Where execution referred to in clause (2) (b) has issued, the amount recoverable from a director is the amount remaining unsatisfied after execution. R.S.O. 1990, c. B.16, s. 131 (3).

Rights of director who pays debt

(4) Where a director pays a debt under subsection (1) that is proved in liquidation and dissolution or bankruptcy proceedings, the director is entitled to any preference that the employee would have been entitled to, and where a judgment has been obtained the director is entitled to an assignment of the judgment. R.S.O. 1990, c. B.16, s. 131 (4).

Idem

(5) A director who has satisfied a claim under this section is entitled to contribution from the other directors who were liable for the claim. R.S.O. 1990, c. B.16, s. 131 (5).

***Employment Standards Act 2000*, S.O. 2000, c. 41**

Section 81

Directors' liability for wages

81. (1) The directors of an employer are jointly and severally liable for wages as provided in this Part if,

(a) the employer is insolvent, the employee has caused a claim for unpaid wages to be filed with the receiver appointed by a court with respect to the employer or with the employer's trustee in bankruptcy and the claim has not been paid;

(b) an employment standards officer has made an order that the employer is liable for wages, unless the amount set out in the order has been paid or the employer has applied to have it reviewed;

(c) an employment standards officer has made an order that a director is liable for wages, unless the amount set out in the order has been paid or the employer or the director has applied to have it reviewed; or

(d) the Board has issued, amended or affirmed an order under section 119, the order, as issued, amended or affirmed, requires the employer or the directors to pay wages and the amount set out in the order has not been paid. 2000, c. 41, s. 81 (1).

Court File No.: 31-OR-207893-T

IN THE MATTER OF THE BANKRUPTCY OF SMP PAPER CORP., OF THE CITY OF SAULT STE. MARIE, PROVINCE OF ONTARIO

ONTARIO
SUPERIOR COURT OF JUSTICE
IN BANKRUPTCY AND INSOLVENCY

Proceeding Commenced at Toronto

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