Court File No. CV-16-11582-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT,* R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF PERFORMANCE SPORTS GROUP LTD., BAUER HOCKEY CORP., BAUER HOCKEY RETAIL CORP., BAUER PERFORMANCE SPORTS UNIFORMS CORP., BPS CANADA INTERMEDIATE CORP., BPS DIAMOND SPORTS CORP., EASTON BASEBALL/SOFTBALL CORP., KBAU HOLDINGS CANADA, INC., PERFORMANCE LACROSSE GROUP CORP., PSG INNOVATION CORP., BAUER HOCKEY RETAIL INC., BAUER HOCKEY, INC., BAUER PERFORMANCE SPORTS UNIFORMS INC., BPS DIAMOND SPORTS INC., BPS US HOLDINGS INC., EASTON BASEBALL/SOFTBALL INC., PERFORMANCE LACROSSE GROUP INC., PSG INNOVATION INC.

(Applicants)

FACTUM OF THE APPLICANTS
(Re: KERP/KEIP Approval)

Dated: January 6, 2017

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TO: THE SERVICE LIST

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PART I - INTRODUCTION

1. Performance Sports Group Ltd. ("**PSG**"), Bauer Hockey Corp., Bauer Hockey Retail Corp., Bauer Performance Sports Uniforms Corp., BPS Canada Intermediate Corp., BPS Diamond Sports Corp., Easton Baseball/Softball Corp., KBAU Holdings Canada, Inc., Performance Lacrosse Group Corp., PSG Innovation Corp., Bauer Hockey Retail Inc., Bauer Hockey, Inc., Bauer Performance Sports Uniforms Inc., BPS Diamond Sports Inc., BPS US Holdings Inc., Easton Baseball/Softball Inc., Performance Lacrosse Group Inc., and PSG Innovation Inc. (collectively, the "**Applicants**" or the "**PSG Entities**") were granted protection from their creditors under the *Companies' Creditors Arrangement Act,* R.S.C. 1985, c. C-36, as amended (the "**CCAA**") pursuant to an Order (as amended and restated, the "**Initial Order**") of this Court (the "**Canadian Court**") dated October 31, 2016. On the same date, the PSG Entities also filed for creditor protection (the "**Chapter 11 Proceedings**") in the United States Bankruptcy Court for the District of Delaware (the "**U.S. Court**" and together with the

Canadian Court, the “**Courts**”) under the U.S. Bankruptcy Code. Ernst & Young Inc. was appointed as monitor (the “**Monitor**”) of the Applicants in these CCAA proceedings (the “**CCAA Proceedings**” and together with the Chapter 11 Proceedings, the “**Restructuring Proceedings**”).

2. This motion is brought by the Applicants seeking an Order substantially in the form of the draft Order included at Tab 3 of the Applicants' Motion Record seeking, among other things:

(a) Approval of the Key Employee Retention Plan (the “**KERP**”) and the Key Employee Incentive Plan (the “**KEIP**”) which provide for retention or incentive bonuses, respectively, to certain highly skilled and experienced employees of the PSG Entities (the “**Key Employees**”) all of which is to be secured by a priority charge (the “**Key Employee Charge**”) on the Applicants' property; and

(b) Sealing the unredacted version of Confidential Exhibit “B” (the “**Confidential Exhibit**”) to the Affidavit of Brian J. Fox sworn January 3, 2017 (the “**KERP/KEIP Affidavit**”) containing certain confidential details about the KERP Participants (defined below).

PART II - THE FACTS

3. The facts with respect to this motion are more fully set out in the KERP/KEIP Affidavit. All capitalized terms used but not defined herein have the meaning given to them in the KERP/KEIP Affidavit.

A. The Development of the KEIP and KERP

4. The Applicants' restructuring strategy includes the going concern sale of substantially all of their assets. Pursuant to that strategy, by orders dated November 30, 2016, the Applicants obtained the Courts' approval of a sales process (the "**Sales Process**") which includes a stalking horse bid and bidding procedures to govern the process.

KERP/KEIP Affidavit at paras. 27, 30, Applicants' Motion Record, Tab 2.

5. It was apparent to the Applicants that certain employees would be critical to preserving value and continuing normal operations during the Sales Process period for the benefit of the Applicants and their stakeholders. In consultation with their advisors, the Applicants identified those employees, being the Key Employees, and developed the KERP and the KEIP in order to retain and incentivize that group.

6. The Key Employees consist of six senior executives, all of whom are "insiders" for the purposes of the U.S. Bankruptcy Code (the "**KEIP Participants**"), and 60 key non-insider employees (the "**KERP Participants**") who occupy essential management and operational roles with the Applicants. All KEIP Participants are employed by the U.S.-incorporated Applicant entities.

KERP/KEIP Affidavit at paras. 15, 27, 30, Applicants' Motion Record, Tab 2.

7. The Key Employees represent a cross-section of various functions at the Applicants' business, including senior management, business development, product/brand management, research and development, design, sales/marketing, finance, human resources, legal, IT, supply chain and operations.

KERP/KEIP Affidavit at paras. 12, 13, Applicants' Motion Record, Tab 2.

i. The KEIP

8. The KEIP provides for incentive payments to the KEIP Participants based on the sales proceeds realized from the Sales Process, after payment of any applicable bid protections (the "**Sale Proceeds**"). This metric was used because the KEIP Participants have control and oversight of the Sales Process.

KERP/KEIP Affidavit at para. 30, Applicants' Motion Record, Tab 2.

9. If the Sale Proceeds exceed the consideration provided under the Stalking Horse Agreement by US$5,000,000, the KEIP Participants will be entitled to Tier 1 "target" payouts of 100% of their target bonuses. The total incentive pool under the Tier 1 "target" level is US$1,776,753, which amounts to an average of US$296,125 per KEIP Participant. If Sale Proceeds exceed the consideration provided under the Stalking Horse Agreement by at least US$50,000,000, the KEIP Participants will be entitled to Tier 2 "stretch" compensation of 200% of their target bonuses. If the Tier 2 "stretch" level is met, the KEIP will have a total plan cost of US$3,553,505, which amounts to an average of US$592,251 per KEIP Participant. If the Sale Proceeds realized by Applicants exceed US$625,000,000, the KEIP Participants will be entitled to an aggregate payout which equals 3% of the total consideration above US$625,000,000 as an additional bonus on top of the Tier 2 "stretch" bonuses.

KERP/KEIP Affidavit at paras. 31, 32; Applicants' Motion Record, Tab 2.

10. The KEIP payouts will be funded with the Sale Proceeds following closing of the sale transaction resulting from the Sales Process and paid within 30 days.

KERP/KEIP Affidavit at para. 34, Applicants' Motion Record, Tab 2.

11. Participants in the KEIP will forfeit their share of the incentive pool if they are terminated for cause – or voluntarily terminate their employment – prior to the closing date of the sale transaction. The forfeited allocation will not be made available to the remaining KEIP Participants. In the event of an involuntarily termination not for cause, participants are entitled to the same share of the KEIP as if they had not been terminated.

KERP/KEIP Affidavit at para. 35, Applicants' Motion Record, Tab 2.

ii. The KERP

12. The KERP provides retention payments to 60 non-insider employees (as classified by the U.S. Bankruptcy Code), with such payments comprising 12.5% to 25% of each participants' annual base salary, with an average of approximately 21%. The level of compensation was based upon the relative importance of each KERP Participant to the Sale Process together with the Applicants' perceived retention risk assigned to such participant.

KERP/KEIP Affidavit at para. 36, Applicants' Motion Record, Tab 2.

13. The estimated cost of the KERP, assuming all KERP Participants remain employed through the Sales Process, is US$1,652,209, which represents an average of US$27,537 per KERP Participant.

KERP/KEIP Affidavit at para. 37, Applicants' Motion Record, Tab 2.

14. To protect the privacy of the KERP Participants and preserve company morale, the names of the KERP Participants, as well as their positions within the company, wage

information, and KERP payments calculated as a percentage of base salary (the "**KERP Participant Information**"), will only be provided to the Courts, the Monitor and certain other key stakeholders.

KERP/KEIP Affidavit at para. 38, Applicants' Motion Record, Tab 2.

15. The termination provisions in the KERP are identical to the termination provisions in the KEIP.

KERP/KEIP Affidavit at para. 39, Applicants' Motion Record, Tab 2.

B. The Key Employee Charge

16. The Applicants contemplate that amounts owing under the KEIP and the KERP would be secured by a charge up to the maximum amount of US$3.4 million (the "**Key Employee Charge**"). Each Key Employee will only obtain the benefit of the Key Employee Charge up to their respective individual entitlements under the KEIP or the KERP.

KERP/KEIP Affidavit at para. 40, Applicants' Motion Record, Tab 2.

17. The proposed priority of the Key Employee Charge will vary depending on the class of collateral in respect of which it is applied.

KERP/KEIP Affidavit at para. 41, Applicants' Motion Record, Tab 2.

C. The Need for the KEIP and KERP

18. Being a retail- and consumer-driven business, the Applicants' vendor, customer and employee relationships are central to the value of the enterprise. Attrition of employees – particularly the Key Employees – erodes value to the detriment of the Applicants' stakeholders.

The Key Employees have also assumed added responsibilities in connection with the Restructuring Proceedings and the Sale Process, such as ensuring compliance of the Applicants' operations with the Stalking Horse Agreement, facilitating and conducting management presentations for potential bidders and responding to bidder information requests.

KERP/KEIP Affidavit at para. 29, Applicants' Motion Record, Tab 2.

19. Since the commencement of the Restructuring Proceedings, three employees originally slated for participation in the KERP have resigned to pursue other employment opportunities, in each instance citing uncertainty and instability in the PSG Entities' operations as one of the reasons for departing. In addition, fifteen other employees have resigned since commencement of the Restructuring Proceedings, and there have been thirty-six employee resignations since June 2016. These departures have put substantial additional demands and pressures on the Key Employees and are illustrative of the issues the Applicants face in retaining Key Employees.

KERP/KEIP Affidavit at para. 26, Applicants' Motion Record, Tab 2.

20. Without the implementation of the KEIP and the KERP, the Key Employees are likely to pursue other employment and may not be motivated to perform to their highest level.

KERP/KEIP Affidavit at para. 43, Applicants' Motion Record, Tab 2.

PART III - ISSUES

21. This motion addresses the following issues:

(a) Should this Court approve the KEIP, the KERP and the Key Employee Charge; and

(b) Should this Court seal the Confidential Exhibit.

PART IV - LAW AND ARGUMENT

A. The KEIP and KERP Should Be Approved and the Key Employee Charge Should Be Granted

i. <u>This Court has the Discretion to Approve the KEIP, the KERP and the Key Employee Charge</u>

22. CCAA courts have discretion to authorize a KEIP and KERP and grant a charge to secure the Applicants' obligations thereunder.

> *Grant Forest Products Inc., (Re)*, 2009 CarswellOnt 4699 [*Grant Forest Products*] at para. 8 (Ont. S.C.J. [Comm. List]), Applicants' Book of Authorities ("BOA"), Tab 1.
>
> *Canwest Global Communications Corp., (Re),* 2009 CarswellOnt 6184 [*Canwest Global*] at para. 49 (Ont. S.C.J. [Comm. List]), Applicants' BOA, Tab 2.

23. KERPs are designed to retain employees who are important to the management and operations of a debtor company at a time when they are likely to look for other employment because of the company's financial distress. KERPs have been approved in numerous CCAA proceedings where the retention of key employees is critical to a successful restructuring. KEIPs focus on providing incentives for key employees to achieve certain milestones who have a significant role in a debtor company's restructuring. KEIPs have been approved by this Court in *Nortel* and *Northstar* with the courts drawing on the same rationale applied to approve KERPs.

> *Nortel Networks Corp. (Re)*, 2009 CarswellOnt 1330 [*Nortel*] at para. 14 (Ont. S.C.J. [Comm. List]), Applicants' BOA, Tab 3.
>
> *Northstar Aerospace Inc. (Re)*, 2012 CarswellOnt 17448 at paras. 4-11 (Ont. S.C.J. [Comm. List]), Applicants' BOA, Tab 4.

24. In *Grant Forest Products*, the Court considered the following factors in approving an employee retention plan and a key employee charge:

(a) Whether the monitor supports the employee retention agreement and the key employee charge;

(b) Whether the beneficiaries of the employee retention plan are likely to consider other employment opportunities if the key employee charge is not approved;

(c) Whether the beneficiaries of the employee retention plan are crucial to the successful restructuring of the debtor company;

(d) Whether a replacement could be found in a timely manner should the beneficiary elect to terminate his or her employment with the debtor company; and

(e) The business judgement of the board of directors of the debtor company.

Grant Forest Products at paras. 8-10, Applicants' BOA, Tab 1.

25. In *Grant Forest Products,* the Court noted that the business judgement of the board of directors of the debtor company and the monitor should rarely be ignored when it comes to approving a KERP and a key employee charge.

Grant Forest Products at para. 18, Applicants' BOA, Tab 1.

26. More recently, in *Target Canada Co.*, the Court approved a KERP and a key employee charge after considering, among others, the following: (a) the factors enumerated in *Grant Forest Products* were satisfied; (b) the size of the KERP was reasonable relative to the total workforce of the debtor companies; (c) the quantum of the KERP was consistent with the relative size of KERPs granted in complex restructurings; and (d) the monitor supported the KERP and was of the view that it was reasonable and appropriate in the circumstances.

Target Canada Co., (Re), 2015 ONSC 303 [*Target*] at paras. 56-59, Applicants' BOA, Tab 5.

ii. <u>The KEIP and KERP Should Be Approved</u>

27. In this instance, the *Grant Forest Products* and *Target* factors have been met:

(a) The Monitor has filed a report supporting the KERP, the KEIP and the Key Employee Charge, concurring with the rationale for the programs;

(b) In developing the KERP, which was done in consultation with their legal and financial advisors, the Applicants considered the retention risk of each of the Key Employees and determined there was such a risk, as further evidenced by the loss of a number of employees prior to and during the Restructuring Proceedings;

(c) The Applicants have selected each of the Key Employees based on their criticality to a successful restructuring of the Applicants' business;

(d) The Key Employees have institutional knowledge and experience which cannot be easily replaced;

(e) The PSG board of directors (the "**PSG Board**"), including all independent directors, approved the Key Employees and the amounts of the cash payments offered to them under the KEIP or KERP; and

(f) The quantum under the KERP and KEIP are reasonable. In developing the KERP and KEIP, Alvarez & Marsal North America LLC compared the KERP and KEIP to fifteen recent incentive programs for comparable companies undergoing insolvency proceedings to ensure the payouts provided thereunder are appropriate in light of the size and complexity of the Applicants' business and restructuring.

KERP/KEIP Affidavit at para. 18-19, 21-22, 24, 26, 47, Applicants' Motion Record, Tab 2.

Fourth Report of the Monitor dated January 5, 2017 at paras. 22 - 26 and 28.

28. Further, the KEIP Participants only include members of the Applicants' senior management team with control and oversight of the Sales Process. The PSG Board believed that the KEIP was critical to align senior management with the success of the Sales Process and motivate senior executives to maximize recovery for the Applicants' stakeholders.

KERP/KEIP Affidavit at para. 20, Applicants' Motion Record, Tab 2.

29. The Applicants also engaged with, and solicited feedback regarding the KERP and KEIP from, two key stakeholders with a significant economic interest in these Restructuring Proceedings, the statutory committee of the unsecured creditors and the statutory committee of equity security holders (collectively, the "**Committees**"). Following negotiations with the Committees, the Applicants made material modifications to the proposed terms of the KERP and KEIP and with the modifications the Applicants were able to obtain the consensus of the Committees.

KERP/KEIP Affidavit at para. 23, Applicants' Motion Record, Tab 2.

30. The extensive review and consideration undertaken by the Applicants and consensus of the Committees further demonstrate that the proposed KEIP and KERP are fair and reasonable in the circumstances. The KEIP and KERP will provide an incentive for the Key Employees to continue to perform their critical roles throughout the restructuring process to the best of their ability, and therefore, are in the best interests of the Applicants and their stakeholders.

KERP/KEIP Affidavit at para. 44, Applicants' Motion Record, Tab 2.

iii. <u>The Key Employee Charge Should Be Approved</u>

31. The security provided by the Key Employee Charge (to the maximum amount of US$3.4 million) will reassure the Key Employees that they will receive their individual entitlements under the KEIP or KERP despite the Applicants' financial distress. Without the assurance, there is a concern the Key Employees may resign prior to the completion of the Applicants' restructuring.

KERP/KEIP Affidavit at para. 47, Applicants' Motion Record, Tab 2.

32. All parties affected by the Key Employee Charge have been or will be given notice of this motion.

B. The Confidential Supplement Should Be Sealed

33. The Applicants have requested that the unredacted version of the Confidential Exhibit, which contains the KERP Participant Information, be sealed unless otherwise ordered by the Court.

34. Pursuant to the Ontario *Courts of Justice Act*, this Court has the discretion to order that any document filed in a civil proceeding be treated as confidential, sealed and not form part of the public record.

Courts of Justice Act, R.S.O. 1990, c. C.4, s. 137(2).

35. In *Sierra Club of Canada v. Canada (Minister of Finance)*, the Supreme Court of Canada adopted the following test to determine when a sealing order should be made:

> A confidentiality order under Rule 151 should only be granted when:

> (a) such an order is necessary in order to prevent serious risk to an important interest, including a commercial interest, in the context of litigation because reasonable alternative measures will not prevent the risk; and
>
> (b) the salutary effects of the confidentiality order, including the effects on the right of civil litigants to a fair trial, outweigh the deleterious effects, including the effects on the right to free expression, which in this context includes the public interest in open and accessible court proceedings.
>
> *Sierra Club of Canada v. Canada (Minister of Finance)*, 2002 SCC 41 at para. 53, Applicant's BOA Tab 6.

36. Orders sealing confidential supplements relating to KERPs containing sensitive personal and compensation information have previously been determined to be appropriate by this Court.

> *Canwest Global* at para. 52, Applicants' BOA, Tab 3.

37. The Confidential Exhibit contains sensitive personal and compensation information about the KERP Participants. Protecting the disclosure of such information (the disclosure of which will cause harm to both the Applicants and the KERP Participants) is an important commercial interest that should be protected. Moreover, the KERP Participants have a reasonable expectation that their names and salary information will be kept confidential.

38. The salutary effects of sealing the Confidential Exhibit – namely the protection of commercially sensitive and personal information that could negatively affect the Applicants and the KERP Participants if disclosed – outweigh any deleterious effect of restricting the accessibility of these court proceedings.

PART V - ORDER REQUESTED

39. For the above reasons, the Applicants request the Court grant an Order substantially in the form of the draft Order included at Tab 3 of the Applicants' Motion Record approving the KEIP, the KERP and the Key Employee Charge and sealing the Confidential Exhibit, among other things.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 6th day of January, 2017.

/s/ *Stikeman Elliott*
Stikeman Elliott LLP

Lawyers for the Applicants

SCHEDULE "A"
LIST OF AUTHORITIES

1. *Grant Forest Products Inc., (Re),* 2009 CarswellOnt 4699 (Ont. S.C.J. [Comm. List]).

2. *Canwest Global Communications Corp., (Re),* 2009 CarswellOnt 6184 (Ont. S.C.J. [Comm. List]).

3. *Nortel Networks Corp., (Re),* 2009 CarswellOnt 1330 (Ont. S.C.J. [Comm. List]).

4. *Northstar Aerospace Inc. (Re),* 2012 CarswellOnt 17448 (Ont. S.C.J. [Comm. List]).

5. *Target Canada Co.*, *Re*, 2015 ONSC 303.

6. *Sierra Club of Canada v. Canada (Minister of Finance)*, 2002 SCC 41.

SCHEDULE "B"
RELEVANT STATUTES

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

11. General power of court

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

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

137. Documents public

Sealing documents

(2) A court may order that any document filed in a civil proceeding before it be treated as confidential, sealed and not form part of the public record.

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