Court File No. CV-24-00722386-00CL

***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 ATLAS GLOBAL BRANDS INC., GREENSEAL CANNABIS COMPANY, LTD., GREENSEAL NURSERY, LTD., AGMEDICA BIOSCIENCE INC., WELLWORTH HEALTH CORP., 5047346 ONTARIO INC., 8050678 CANADA INC. AND TAVIVAT NATURALS INC.**

Applicants

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# FACTUM OF THE ATTORNEY GENERAL OF CANADA
# (ARVO Approval)

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**ATTORNEY GENERAL OF CANADA**
Department of Justice
120 Adelaide Street West
Suite 400
Toronto, Ontario
M5H 1T1

**Kevin Dias**
Tel: 647-256-7360
Fax: 416-973-0810
Email: Kevin.Dias@justice.gc.ca
LSO #: 39035N

**Edward Park**
Tel: 647-292-9368
Fax: 416-973-0810
Email: Edward.Park@justice.gc.ca
LSO #: 45496L

TO : SERVICE LIST

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## PART I : OVERVIEW

1. The Applicants seek to vest out a source deduction deemed trust claim in the amount of **$1,772,417.69** (the "**Source Deduction Deemed Trust**") by way of a reverse vesting transaction ("**RVO**").

2. The Attorney General of Canada opposes the requested relief. Vesting out a trust claim through an RVO – in and of itself, an extraordinary remedy – would be an extraordinary result. The sanctity of trust claims should be unequivocally affirmed and preserved by this Honourable Court.

3. While the Court has broad discretion under section 11 of the *Companies' Creditors Arrangement Act* ("***CCAA***"),[1] it is respectfully submitted that issuing an RVO in this case would be inappropriate. The proposed RVO would create inconsistency with subsection 6(3) of the *CCAA*, which requires payment in full of a source deduction liability under a *CCAA* plan, along with subsection 37(2) of the CCAA which preserves the Source Deduction Deemed Trust in *CCAA*. Although there is no plan of compromise or arrangement in the current case, permitting a source deduction liability to be vested out through an RVO within a *CCAA* proceeding would create disharmony and asymmetry between a *CCAA* plan and *CCAA* RVO. The transaction vehicle of choice should be "source deduction neutral", and there should be equality of treatment of the source deduction liability between a *CCAA* plan and *CCAA* RVO.

4. When viewed through the lens of *Third Eye Capital Corporation*,[2] the test for determining whether the interest of a third party should be extinguished through a vesting order has also not been satisfied in that:

   (i) a statutory trust claim is one of the highest claims known to the common law; and

   (ii) the Crown has not consented in any manner whatsoever to having its trust claim extinguished and, to the contrary, was expecting to be paid the exact same trust fund amounts that were used to keep the Atlas enterprise afloat

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[1] *Companies' Creditors Arrangement Act*, RSC 1985, c. C-36.

[2] *Third Eye Capital Corporation v. Resources Dianor Inc./Dianor Resources Inc.*, 2019 ONCA 508.

prior to the initiation of the CCAA proceedings. The trust funds were effectively used as working capital by the Applicants, akin to a "Pre-CCAA DIP Loan", with the Crown acting as an involuntary creditor.

5. The Crown is also in a worse position under the proposed RVO than under the presumed alternative, bankruptcy, in that recourse against the directors will effectively be foreclosed under the proposed RVO whereas the Crown would still have recourse against the directors in a bankruptcy scenario (subject to any due diligence defences). It is important to note that bankruptcy is not the desired result here. Payment of the source deduction liability and affirmation of the sanctity of trust claims is the desired result.

6. Finally, the Applicants are asking this Honourable Court to approve a binding letter of intent pursuant to which "a draft Purchase Agreement"[3] will be executed at a later date "on substantially the terms of the Binding LOI".[4] The absence of the share purchase agreement from the record does not afford the supervising Judge the opportunity to scrutinize the agreement on its final terms, which is also unfair to the stakeholders.

[3] Affidavit of Jason Cervi sworn September 29, 2024 para. 72 (**"Cervi Affidavit"**).

[4] Cervi Affidavit at para. 72.

## PART II : FACTS

7. The Crown relies on the affidavit of Sandra Palma sworn on October 1, 2024 (**"Palma Affidavit"**). Any capitalized terms not defined herein has the same meaning ascribed to them in Palma Affidavit.

8. The Crown also relies on the written reasons of this Honourable Court released on July 11, 2024, further to which it was noted that "[t]his is not Atlas and AgMedica's first journey down the CCAA road".[5]

9. Indeed, certain of the Applicants herein previously compromised almost $1.1 million in tax liabilities during their first CCAA proceeding in 2019.[6] Under the proposed RVO, AgMedica would vest out its payment obligations to the Crown under the first *CCAA* restructuring.[7]

10. Since restructuring in 2019, as evidenced by Exhibits "A" and "B" to the Palma Affidavit, the Applicants quickly fell back into tax non-compliance with unfiled returns beginning as early as 2020 and continuing through to 2024 up to the date of filing under the CCAA.[8]

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[5] *Atlas Global Brands Inc. et al. v. The Attorney General of Canada on Behalf of His Majesty the King in Right of Canada as represented by the Minister of National Revenue* (11 July 2024), Toronto CV-24-00722386-00CL/CV-24-00722700-00CL/CV-24-00722799-00CL, ONSC.

[6] Palma Affidavit, para. 12.

[7] Cervi Affidavit, para. 88.

[8] Palma Affidavit, paras. 2 and 3.

11. In addition to systematic failings to meet its filing obligations, the Applicants also fell into arrears across multiple tax accounts, accumulating excise duty arrears of over $3.7 million by AgMedica BioScience for periods from 2022-2024 and over $3 million in excise duty arrears for GreenSeal for the 2023-2024 pre-filing period.[9]

12. Perhaps most notably, AgMedica Bioscience failed to remit employee withholdings totaling $1,772,417.69 in 2023 and 2024 in respect of which an assessment of $2,109,991.44 was assessed on September 18, 2024 following a CRA trust examination.

13. The trust examination to determine source deduction arrears for GreenSeal Cannabis is pending, as the CRA awaits requested payroll records to be provided by GreenSeal.

14. Therefore, in the months preceding a second *CCAA* filing, AgMedica failed to remit more than $1.7 million of source deductions which were deducted from its employees' remuneration.[10]

15. The CRA has never consented or acquiesced to the Source Deduction Deemed Trust being vested out.[11]

[9] Palma Affidavit, para. 3.

[10] Palma Affidavit, paragraphs 5, 8, 9 and 10.

[11] Palma Affidavit, paragraphs 6.

## PART III : LAW

### A. Importance of Source Deductions to Public Finance

16. Employee source deductions are the cornerstone of the tax collection system in Canada.[12] In *First Vancouver*,[13] the Supreme Court of Canada recognized that the collection of source deductions remains "at the heart" of public finance in Canada.

17. The *Income Tax Act* (**"*ITA*"**)[14] and other federal statutes require employers to withhold income taxes and other amounts from employee remuneration and to remit those amounts to the Crown. Those withholdings form part of the gross wages of an employee and are credited against the tax payable of an employee regardless of whether the employer actually remits them.

18. Employee withholdings are not the property of an employer. When an employer utilizes withholdings to increase liquidity and working capital, the Crown becomes an involuntary creditor.

19. Because of the importance of collecting source deductions, the *ITA, Canada Pension Plan* ("***CPP***"),[15] and *Employment Insurance Act* ("***EIA***")[16] give the Minister the vehicle

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[12] Source deductions comprise a significant portion of the annual tax revenues. They also fund social programs like the Canada Pension Plan and Employment Insurance.

[13] *First Vancouver Finance v MNR*, 2002 SCC 49 at para. 22.

[14] *Income Tax Act*, RSC 1985, c. 1 (5th Supp.).

[15] *Canada Pension Plan*, RSC 1985, c. C-8.

[16] *Employment Insurance Act*, SC 1996, c. 23.

of a deemed trust to recover employee tax deductions which employers fail to remit.[17] The deemed trust provisions are found at:

(i) subsection 227(4) of the *ITA*;

(ii) subsection 86(2) of the *EIA*; and

(iii) subsection 23(3) of the *CPP*.

20. The deemed trust operates in two stages. First, subsection 227(4) of the *ITA* deems the amounts that an employer withholds from remuneration paid to employees to be held in trust for the benefit of the Crown. Second, if the employer fails to remit those amounts when due, subsection 227(4.1) of the *ITA* deems all property of the employer to be held in trust for the Crown in an amount equal to the failed remittance.

21. Furthermore, subsection 37(1) of the *CCCA* nullifies Crown deemed trusts in *CCAA* proceedings, **except** that subsection 37(2) of the *CCAA* specifically preserves the deemed trust for source deductions under the *ITA*, *EIA,* and *CPP*. Subsection 37(2) of the *CCAA* represents the effort of Parliament, after many years of legislative evolution, to balance the competing policy goals of tax collection and corporate restructuring.

22. Therefore, Parliament has embedded the primacy of source deductions into the *CCAA*, *ITA*, *EIA* and *CPP*. These statutes work in harmony to ensure that the deemed trust for unremitted source deductions remains paramount.

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[17] *First Vancouver* at para. 22.

23. Finally, under subsection 6(3) of the *CCAA*, the Court may only sanction a compromise or arrangement if that provides for payment in full to the Crown, within six months, of all amounts that were outstanding at the time of the application included in the deemed trusts. Only the consent of the Crown can remove that restriction.

## B. Inconsistent Result

24. Courts supervising a *CCAA* reorganization have the authority to make orders that facilitate the restructuring process. Indeed, one of the salient features of the *CCAA* is the broad discretionary power it vests in the supervising court.[18] This jurisdiction is constrained only by restrictions set out in the *CCAA* itself and the requirement that the order made be appropriate in the circumstances.[19]

25. Although there is no plan of compromise or arrangement in the current case, permitting a source deduction liability to be vested out through an RVO within a *CCAA* proceeding creates disharmony and asymmetry between a *CCAA* plan and *CCAA* RVO. It is for this reason that the Crown respectfully submits that the proposed RVO is inappropriate. The transaction vehicle of choice should be "source deduction neutral", and there should be equality of treatment of the source deduction liability between a *CCAA* plan and *CCAA* RVO.

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[18] *9354-9186 Québec inc. v Callidus Capital Corp.,* 2020 SCC 10 at paras. 47-48 (**"*Callidus Capital*"**).

[19] *Century Services Inc. v Canada (Attorney General),* 2010 SCC 60 at para. 68-70 (**"*Century Services*"**); see also *Callidus Capital* at para. 48.

26. Parliament was wholly aware that the purpose of the CCAA is to avoid the social and economic consequences of bankruptcy, **yet** Parliament still required that source deduction debts not be extinguished.

## C. The *Third Eye* Test

27. In *CannaPiece*,[20] Mr. Justice Osborne declined to approve an RVO that would have vested out the interest of a first-ranking secured creditor. In so doing, His Honour referenced the Ontario Court of Appeal decision in *Third Eye* and the decision of Mr. Justice Penny in *Harte Gold*.[21] As Mr. Justice Osborne wrote at paragraphs 55 to 58 of *CannaPiece* (citations omitted):

> 55. The Court of Appeal for Ontario considered in *Third Eye Capital Corporation v. Dianor Resources Inc.*, ("*Third Eye*") what it described as a "cascading analysis" of the factors to be considered when determining whether a third party interest should be extinguished in a vesting order:
>
> > (a) first, the nature and strength of the interest that is proposed to be extinguished;
> >
> > (b) second, whether the interest holder has consented to the vesting out of their interest either in the insolvency process itself or in agreements reached prior to the insolvency; and
> >
> > (c) third, if the first two steps proved to be ambiguous or inconclusive, a consideration of the equities to determine if a vesting order is appropriate in the circumstances.
>
> 56. A consideration of the equities contemplated in the third step includes consideration of the prejudice, if any, to the third party interest holder; whether the third party may be adequately compensated for its

[20] *In the Matter of the Companies' Creditors Arrangement Act* and *in the Matter of CannaPiece Group Inc.*, 2023 ONSC 841.

[21] *Harte Gold Corp. (Re)*, 2022 ONSC 653.

> interest from the proceeds of the disposition are sale; whether, based on evidence of value, there is any equity in the property; and whether the parties are acting in good faith.
>
> 57. Finally, Penny, J. considered the factors applicable to a determination of whether a reverse vesting order should be approved, in *Harte Gold Corp. (Re)*. In that case, the Court considered the s.36(3) factors set out above, "making provision or adjustment, as appropriate, for the unique aspects of a reverse vesting transaction" since the very nature of a reverse vesting order is such that it does not contemplate a typical sale of assets.
>
> 58. Justice Penny observed that a reverse vesting order was both an equitable and an extraordinary remedy, and one that ought not to be regarded as the "norm" and concluded that the following factors are applicable to consideration of whether a reverse vesting order is appropriate in the circumstances:
>
> (a) Why is the RVO necessary in this case?
>
> (b) Does the RVO structure produce an economic result at least as favourable as any other viable alternative?
>
> (c) Is any stakeholder worse off under the RVO structure then they would have been under any other viable alternative? and
>
> (d) does the consideration being paid for the debtor's business reflect the importance and value of the licenses and permits (or other intangible assets) being preserved under the RVO structure[22]

28. Applying *Third Eye* to the present matter, the Applicant seeks to extinguish a statutory trust claim which is one of the highest claims known to the common law. The Source Deduction Deemed Trust ranks ahead of all secured creditors — other than mortgagees with a registered interest in land that pre-date the failure to remit the source deductions,

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[22] *CannaPiece* at paras. 55-58.

subject to certain grind down rules. If, in *CannaPiece*, this Court did not permit a first-ranking secured creditor to be vested out, the law should not permit an even higher-ranked claim to be extinguished.

29. The Crown has not consented in any manner whatsoever to having its trust claim extinguished and, to the contrary, was expecting to be paid the exact same trust fund amounts that were used to keep the Atlas enterprise afloat prior to the initiation of the CCAA proceedings. The trust funds were effectively used as working capital by the Applicants, akin to a "Pre-CCAA DIP Loan", with the Crown acting as an involuntary creditor.

## D. Crown is in a worse position

30. Considering factors (b) and (c) from *Harte Gold* (referenced in paragraph 58 of *CannaPiece*, above), the Crown is in a worse position under this proposed RVO than under a bankruptcy because the RVO will effectively foreclose recourse against the directors whereas the Crown would still have recourse against the directors in a bankruptcy scenario (subject to any due diligence defences). It is important to note that bankruptcy is not the desired result here. Payment of the source deduction liability and affirmation of the sanctity of trust claims is the desired result.

31. The director's liability provisions are found at:

(i) *ITA*, section 227.1;

(ii) *Excise Tax Act*, section 323;[23] and

(iii) *Excise Act, 2001*, section 295.[24]

## E. Deficient Record

32. The Applicants are asking this Honourable Court to approve a binding letter of intent pursuant to which "a draft Purchase Agreement"[25] will be executed at a later date "on substantially the terms of the Binding LOI". [26] The absence of the share purchase agreement from the record does not afford the supervising Judge the opportunity to scrutinize the agreement on its final terms, which is also unfair to the stakeholders.

## PART IV: RELIEF SOUGHT

33. That the motion be dismissed.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED**

Dated October 3, 2024

*Attorney General of Canada*

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[23] *Excise Tax Act*, RSC 1985, c. E-15.

[24] *Excise Act, 2001*, SC 2002, c. 22.

[25] Cervi Affidavit at para. 72.

[26] Cervi Affidavit at para. 72.

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***ONTARIO***
**SUPERIOR COURT OF JUSTICE**

Proceeding Commenced at Toronto

# FACTUM OF THE ATTORNEY GENERAL OF CANADA


**ATTORNEY GENERAL OF CANADA**
Department of Justice
120 Adelaide Street West
Suite 400
Toronto, Ontario
M5H 1T1

Per : **Kevin Dias/Edward Park**
Tel : 647-256-7360/647-292-9368
Fax : 416-973-0810
Email : Kevin.Dias@justice.gc.ca
Edward.Park@justice.gc.ca
LSO #: 39035N/45496L

Lawyers for the Canada Revenue Agency