

COURT OF APPEAL FOR ONTARIO

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 Grant Forest Products Inc., Grant Alberta
Inc., Grant Forest Products Inc., and Grant U.S. Holdings
GP

Applicants

**BOOK OF AUTHORITIES
OF THE MONITOR**

November 3, 2009

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TAB 1

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In the Matter of the Companies' Creditors Arrangement Act, R.S.C.
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In the Matter of Canadian Airlines Corporation and Canadian Airlines
International Ltd.

Resurgence Asset Management LLC, Applicant and Canadian Airlines
Corporation and Canadian Airlines International Ltd., Respondents

Alberta Court of Appeal [In Chambers]

Wittmann J.A.

Heard: May 18, 2000

Judgment: May 29, 2000

Docket: Calgary Appeal 00-18816, 2000 ABCA 149

D. Haigh, Q.C., and *D. Nishimura*, for Applicant.

A.L. Friend, Q.C., and *H.M. Kay, Q.C.*, for Respondents.

S. Dunphy, for Air Canada.

A.J. McConnell, for Bank of Nova Scotia Trust Company of New York and
Montreal Trust Co. of Canada.

P.T. McCarthy, Q.C., for Price Waterhouse Coopers.

Corporations — Arrangements and compromises — Under Companies' Creditors Arrangement Act — Miscellaneous issues — Applicant was unsecured creditor of C Corp. — Board appointed by A Corp. caused C Corp. to commence proceedings under CCAA under which A Corp. stood to gain substantial benefits — Proposed plan of compromise and arrangement filed under Act — Order made that classification of creditors not be fragmented to exclude A Corp. as separate class from applicant in terms of unsecured creditors, that A Corp. be entitled to vote on plan pursuant to s. 6 of Act, that there be no separation of unsecured creditors of two divisions of C Corp. for voting purposes, and that votes in respect of claims assigned to A Corp. be recorded and tabulated separately for purpose of consideration in application for court approval of plan — Applicant brought application for leave to appeal that order — Application dismissed — Decisions of supervising judge under Act entitled to considerable deference — Person seeking leave to appeal required to show error in principle of law or palpable and overriding error of fact — Exercise of discretion by reviewing judge not subject to review so long as discretion exercised judicially — Reviewing judge made no error of law — Applicant failed to make out prima facie meritorious case — Granting of leave would likely unduly hinder progress of action — Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 6.

Cases considered by Wittmann J.A.:

- Blue Range Resource Corp., Re* (1999), 244 A.R. 103, 209 W.A.C. 103, 12 C.B.R. (4th) 186 (Alta. C.A.) — referred to
- Blue Range Resource Corp., Re*, (sub nom. *Blue Range Resources Corp., Re*) 250 A.R. 172, (sub nom. *Blue Range Resources Corp., Re*) 213 W.A.C. 172, 15 C.B.R. (4th) 160, 2000 ABCA 3 (Alta. C.A. [In Chambers]) — referred to
- Blue Range Resource Corp., Re* (2000), (sub nom. *Blue Range Resources Corp., Re*) 250 A.R. 239, (sub nom. *Blue Range Resources Corp., Re*) 213 W.A.C. 239, 15 C.B.R. (4th) 192 (Alta. C.A. [In Chambers]) — referred to
- Fairview Industries Ltd., Re* (1991), 11 C.B.R. (3d) 71, (sub nom. *Fairview Industries Ltd., Re* (No. 3)) 109 N.S.R. (2d) 32, (sub nom. *Fairview Industries Ltd., Re* (No. 3)) 297 A.P.R. 32 (N.S. T.D.) — referred to
- Med Finance Co. S.A. v. Bank of Montreal* (1993), 24 B.C.A.C. 318, 40 W.A.C. 318, 22 C.B.R. (3d) 279 (B.C. C.A.) — referred to
- Multitech Warehouse Direct Inc., Re* (1995), 32 Alta. L.R. (3d) 62 (Alta. C.A.) — referred to
- Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd.* (1988), 64 Alta. L.R. (2d) 139, [1989] 2 W.W.R. 566, 72 C.B.R. (N.S.) 20, 72 C.R. (N.S.) 20 (Alta. Q.B.) — referred to
- Northland Properties Ltd., Re* (1988), 31 B.C.L.R. (2d) 35, 73 C.B.R. (N.S.) 166 (B.C. S.C.) — referred to
- Northland Properties Ltd. v. Excelsior Life Insurance Co. of Canada*, 34 B.C.L.R. (2d) 122, 73 C.B.R. (N.S.) 195, [1989] 3 W.W.R. 363 (B.C. C.A.) — referred to
- NsC Diesel Power Inc., Re* (1990), 79 C.B.R. (N.S.) 1, 97 N.S.R. (2d) 295, 258 A.P.R. 295 (N.S. T.D.) — referred to
- Pacific National Lease Holding Corp., Re* (1992), 72 B.C.L.R. (2d) 368, 19 B.C.A.C. 134, 34 W.A.C. 134, 15 C.B.R. (3d) 265 (B.C. C.A. [In Chambers]) — considered
- Power Consolidated (China) Pulp Inc. v. British Columbia Resources Investment Corp.* (1988), 19 C.P.C. (3d) 396 (B.C. C.A.) — referred to
- Royal Bank v. Fracmaster Ltd.* (1999), (sub nom. *UTI Energy Corp. v. Fracmaster Ltd.*) 244 A.R. 93, (sub nom. *UTI Energy Corp. v. Fracmaster Ltd.*) 209 W.A.C. 93, 11 C.B.R. (4th) 230 (Alta. C.A.) — considered
- Savage v. Amoco Acquisition Co.* (1988), 59 Alta. L.R. (2d) 260, 68 C.B.R. (N.S.) 154, 40 B.L.R. 188, (sub nom. *Amoco Acquisition Co. v. Savage*) 87 A.R. 321 (Alta. C.A.) — referred to
- Sklär-Peppler Furniture Corp. v. Bank of Nova Scotia* (1991), 8 C.B.R. (3d) 312, 86 D.L.R. (4th) 621 (Ont. Gen. Div.) — referred to
- Smoky River Coal Ltd., Re*, (sub nom. *Luscar Ltd. v. Smoky River Coal Ltd.*) 237 A.R. 83, (sub nom. *Luscar Ltd. v. Smoky River Coal Ltd.*) 197 W.A.C. 83, 1999 ABCA 62 (Alta. C.A.) — referred to
- Smoky River Coal Ltd., Re*, 175 D.L.R. (4th) 703, 237 A.R. 326, 197 W.A.C. 326, 71 Alta. L.R. (3d) 1, [1999] 11 W.W.R. 734, 12 C.B.R. (4th) 94 (Alta. C.A.) — considered
- Sovereign Life Assurance Co. v. Dodd* (1891), [1891-4] All E.R. Rep. 246, [1892] 2 Q.B. 573 (Eng. C.A.) — referred to
- Wellington Building Corp., Re*, 16 C.B.R. 48, [1934] O.R. 653, [1934] 4 D.L.R. 626 (Ont. S.C.) — referred to

Woodward's Ltd., Re (1993), 20 C.B.R. (3d) 74, 84 B.C.L.R. (2d) 206 (B.C. S.C.) — referred to

Statutes considered:

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

- s. 2 "secured creditor" — considered
- s. 2 "unsecured creditor" — considered
- s. 4 — considered
- s. 5 — considered
- s. 6 — considered
- s. 6(a) — considered
- s. 6(b) — considered
- s. 13 — considered

APPLICATION for leave to appeal from judgment reported at (2000), 19 C.B.R. (4th) 12 (Alta. Q.B.).

Memorandum of decision. Wittmann J.A.:

Introduction

- 1 This is an application for leave to appeal the decision of Paperny, J. made on May 12, 2000, pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (CCAA). The applicant, Resurgence Asset Management LLC (Resurgence), is an unsecured creditor by virtue of its holding 58.2 per cent of U.S. \$100,000,000.00 unsecured notes issued by Canadian Airlines Corporation (CAC)
- 2 CAC and Canadian Airlines International Ltd. (CAIL) (collectively Canadian) commenced proceedings under the CCAA on March 24, 2000.
- 3 A proposed Plan of Compromise and Arrangement (the Plan) has been filed in this matter regarding CAC and CAIL, pursuant to the CCAA.
- 4 The decision of Paperny, J. May 12, 2000 (the Decision) ordered, among other things, that the classification of creditors not be fragmented to exclude Air Canada as a separate class from Resurgence in terms of the unsecured creditors; that Air Canada should be entitled to vote on the Plan pursuant to s. 6 of the CCAA at the creditors' meeting to be held May 26, 2000; that there be no separation of unsecured creditors of CAC from unsecured creditors of CAIL for voting purposes; and that votes in respect of claims assigned to Air Canada, be recorded and tabulated separately, for the purpose of consideration in the application for court approval of the Plan (the Fairness Hearing).

Leave to Appeal Under the CCAA

- 5 The section of the CCAA governing appeals to this Court is as follows:
 - 13. Except in the Yukon Territory, any person dissatisfied with an order or a decision made under this Act may appeal therefrom on obtaining leave of the

judge appealed from or of the court or a judge of the court to which the appeal lies and on such terms as to security and in other respects as the judge or court directs.

6 The criterion to be applied in an application for leave to appeal pursuant to the CCAA is not in dispute. The general criterion is embodied in the concept that there must be serious and arguable grounds that are of real and significant interest to the parties: *Re Multitech Warehouse Direct Inc.* (1995), 32 Alta. L.R. (3d) 62 (Alta. C.A.) at 63; *Re Smoky River Coal Ltd.* (1999), 237 A.R. 83 (Alta. C.A.); *Re Blue Range Resource Corp.* (1999), 244 A.R. 103 (Alta. C.A.); *Re Blue Range Resource Corp.* (2000), 15 C.B.R. (4th) 160 (Alta. C.A. [In Chambers]); *Re Blue Range Resource Corp.* (2000), 15 C.B.R. (4th) 192 (Alta. C.A. [In Chambers]).

7 Subsumed in the general criterion are four applicable elements which originated in *Power Consolidated (China) Pulp Inc. v. British Columbia Resources Investment Corp.* (1988), 19 C.P.C. (3d) 396 (B.C. C.A.), and were adopted in *Med Finance Co. S.A. v. Bank of Montreal* (1993), 22 C.B.R. (3d) 279 (B.C. C.A.). McLachlin, J.A. (as she then was) set forth the elements in *Power Consolidated* as follows at p.397:

- (1) whether the point on appeal is of significance to the practice;
- (2) whether the point raised is of significance to the action itself;
- (3) whether the appeal is *prima facie* meritorious or, on the other hand, whether it is frivolous; and
- (4) whether the appeal will unduly hinder the progress of the action.

These elements have been considered and applied by this Court, and were not in dispute before me as proper elements of the applicable criterion.

Facts

8 On or about October 19, 1999, Air Canada announced its intention to make a bid for CAC and to proceed to complete a merger subject to a restructuring of Canadian's debt. On or about November 5, 1999, following a ruling by the Quebec Superior Court, a competing offer by Airline Industry Revitalization Co. Inc. was withdrawn and Air Canada indicated that it would proceed with its offer for CAC.

9 On or about November 11, 1999, Air Canada caused the incorporation of 853350 Alberta Ltd. (853350), for the sole purpose of acquiring the majority of the shares of CAC. At the time of incorporation, Air Canada held 10 per cent of the shares of 853350. Paul Farrar, among others, holds the remaining 90 per cent of the shares of 853350.

10 On or about November 11, 1999, Air Canada, through 853350, offered to purchase the outstanding shares of CAC at a price of \$2.00 per share for a total

of \$92,000,000.00 for all of the issued and outstanding voting and non-voting shares of CAC.

- 11 On or about January 4, 2000, Air Canada and 853350 acquired 82 per cent of CAC's outstanding common shares for approximately \$75,000,000.00 plus the preferred shares of CAIL for a purchase price of \$59,000,000.00. Air Canada then replaced the Board of Directors of CAC with its own nominees.
- 12 Substantially all of the aircraft making up the fleet of Canadian are held by Air Canada through lease arrangements with various lessors or other aircraft financial agencies. These arrangements were the result of negotiations with lessors, jointly conducted by Air Canada and Canadian.
- 13 In general, these arrangements include the following:
 - (i) the leases have been renegotiated to reflect contemporary fair market value (or below) based on two independent desk top valuations; and
 - (ii) the present value of the difference between the financial terms under the previous lease arrangements and the renegotiated fair market value terms was characterized as "unsecured deficiency," reflected in a Promissory Note payable to the lessor from Canadian and assigned by the lessor to Air Canada.
- 14 In the result, Air Canada has acquired or is in the process of acquiring all but eight of the deficiency claims of aircraft lessors or financiers listed in Schedule "B" to the Plan in the total amount of \$253,506,944.00. Air Canada intends to vote those claims as an unsecured creditor under the Plan.
- 15 The executory contracts claims listed in Schedule "B" to the Plan total \$110,677,000.00, of which \$108,907,000.00 is the claim of Loyalty Management Group Canada Inc. (Loyalty), an entity with a long term contract with Canadian to purchase air miles. The claim is subject to an agreement of settlement between Loyalty, Canadian and Air Canada. Air Canada was assigned the Loyalty unsecured claim.
- 16 In the Plan, all unsecured creditors of both CAC and CAI are grouped in the same class for voting purposes.
- 17 Pursuant to the Plan, unsecured creditors will receive a payment of \$0.12 on the dollar for each \$1.00 of their claim unless the total amount of unsecured claims exceeds \$800 million, in which case, they will receive less. Air Canada will fund this Pro Rata Cash Amount. As a result of the assignments of the deficiency amounts in favour of Air Canada, if the Plan is approved, Air Canada will notionally be paying a substantial proportion of the Pro Rata Cash Amount to itself.
- 18 The Plan further contemplates Air Canada becoming the 100 per cent owner of Canadian through 853350.
- 19 On April 7, 2000, an Order was granted by Paperny, J., directing that the Plan be filed by the Petitioners; establishing a claims dispute process; authoriz-

ing the calling of meetings for affected creditors to vote on the Plan to be held on May 26, 2000; authorizing the Petitioners to make application for an Order sanctioning the Plan on June 5, 2000; and providing other directions.

- 20 The April 7, 2000 Order established three classes of creditors: (a) the holders of Canadian Airlines Corporation 10 per cent Senior Secured Notes due 2005 (the Secured Noteholders); (b) the secured creditors of the Petitioners affected by the Plan (the Affected Secured Creditors); and (c) the unsecured creditors affected by the Plan (the Affected Unsecured Creditors).
- 21 On April 25, 2000, the Petitioners filed and served the Plan, in accordance with the Order of April 7, 2000. By Notice of Motion dated April 27, 2000, Resurgence brought an application, among other things, seeking "directions as to the classification and voting rights of the creditors ... (and) the quantum of the 'deficiency claims' assigned to Air Canada." Resurgence sought to have Air Canada excluded from voting as an unsecured creditor unless segregated into a separate class. Resurgence also sought to have the holders of the unsecured notes vote as a separate class.
- 22 The result of the April 27, 2000 motion by Resurgence is the Decision.

The Decision

- 23 In the Decision, the supervising chambers judge referred to her order of April 14, 2000, wherein she approved transactions involving the re-negotiation of the aircraft leases. She referred to "about \$200,000,000.00 worth of concessions for CAIL" as "concessions or deficiency claims" which were quantified and reflected in promissory notes which were assigned to Air Canada in exchange for its guarantee of the aircraft leases. The monitor approved of the method of quantifying the claims and Paperny, J. approved the transactions, reserving the issue of classification and voting to her May 12 Decision.
- 24 The Plan provides for one class of unsecured creditor. The unsecured class is composed of a number of types of unsecured claims including executory contracts (e.g. Air Canada from Loyalty) unsecured notes (e.g. Resurgence), aircraft leases (e.g. Air Canada from lessors), litigation claims, real estate leases and the deficiencies, if any, of the senior secured noteholders.
- 25 In seeking to have Air Canada vote the promissory notes in a separate class Resurgence argued several factors before Paperny, J., as set out at pp. 4-5 of the Decision as follows:
1. The Air Canada appointed board caused Canadian to enter into these CCAA proceedings under which Air Canada stands to gain substantial benefits in its own operations and in the merged operations and ownership contemplated after the compromise of debts under the plan.
 2. Air Canada is providing the fund of money to be distributed to the Affected Unsecured Creditors and will, therefore, end up paying itself a portion

of that money if it is included in the Affected Unsecured Creditors' class and permitted to vote.

3. Air Canada gave no real consideration in acquiring the deficiency claims and manufactured them only to secure a 'yes' vote.

26 She then recited the argument made by Air Canada and Canadian to the effect that the legal rights associated with Air Canada's unsecured claims are the same as those associated with the other affected unsecured claimants, and that the matters raised by Resurgence relating to classification are really matters of fairness more appropriately dealt with in a Fairness Hearing scheduled to be held June 5, 2000.

27 After observing that the CCAA offers no guidance with respect to the classification of claims, beyond identifying secured and unsecured categories and the possibility of classes within each category, and that the process has developed in case law, Paperny, J. embarked on a detailed analysis and consideration of the case law in this area including *Norcen Energy Resources Ltd. v. Oakwood Petroleum Ltd.* (1988), 72 C.B.R. (N.S.) 20 (Alta. Q.B.); *Sovereign Life Assurance Co. v. Dodd* (1891), [1892] 2 Q.B. 573 (Eng. C.A.); *Re Fairview Industries Ltd.* (1991), 11 C.B.R. (3d) 71 (N.S. T.D.); *Northland Properties Ltd. v. Excelsior Life Insurance Co. of Canada* (1989), 73 C.B.R. (N.S.) 195 (B.C. C.A.); *Savage v. Amoco Acquisition Co.* (1988), 68 C.B.R. (N.S.) 154 (Alta. C.A.); *Re Woodward's Ltd.* (1993), 84 B.C.L.R. (2d) 206 (B.C. S.C.); *Sklar-Peppler Furniture Corp. v. Bank of Nova Scotia* (1991), 86 D.L.R. (4th) 621 (Ont. Gen. Div.) at 626; *Re NsC Diesel Power Inc.* (1990), 79 C.B.R. (N.S.) 1 (N.S. T.D.); *Re Wellington Building Corp.*, [1934] O.R. 653, 16 C.B.R. 48 (Ont. S.C.). Paperny, J. also referred to an oft-cited article "Reorganization under the Companies Creditors Arrangement Act" by S. E. Edwards (1947), 25 Can. Bar Rev. 587. She concluded her legal analysis at pp.12-13 by setting forth the principles she found to be applicable in assessing commonality of interest as an appropriate test for the classification of creditors:

1. Commonality of interest should be viewed on the basis of the non-fragmentation test, not on an identity of interest test;
2. The interests to be considered are the legal interests the creditor holds qua creditor in relationship to the debtor company, prior to and under the plan as well as on liquidation;
3. The commonality of these interests are to be viewed purposively, bearing in mind the object of the CCAA, namely to facilitate reorganizations if at all possible;
4. In placing a broad and purposive interpretation on the CCAA, the court should be careful to resist classification approaches which would potentially jeopardize potentially viable plans.
5. Absent bad faith, the motivations of the creditors to approve or disapprove are irrelevant.

6. The requirement of creditors being able to consult together means being able to assess their legal entitlement as creditors before or after the plan in a similar manner.

The Standard of Review and Leave Applications

- 28 The elements of the general criterion cannot be properly considered in a leave application without regard to the standard of review that this Court applies to appeals under the CCAA. If leave to appeal were to be granted, the applicable standard of review is succinctly set forth by Fruman, J.A. in *Royal Bank v. Fracmaster Ltd.* (1999), 244 A.R. 93 (Alta. C.A.) where she stated for the Court at p.95:

.... this is a court of review. It is not our task to reconsider the merits of the various offers and decide which proposal might be best. The decisions made by the Chambers judge involve a good measure of discretion, and are owed considerable deference. Whether or not we agree, we will only interfere if we conclude that she acted unreasonably, erred in principle or made a manifest error.

In another recent CCAA case from this Court, *Re Smoky River Coal Ltd.* (1999), 237 A.R. 326 (Alta. C.A.), Hunt, J.A., speaking for the unanimous Court, extensively reviewed the history and purpose of the CCAA, and observed at p.341:

The fact that an appeal lies only with leave of an appellate court (s. 13 CCAA) suggests that Parliament, mindful that CCAA cases often require quick decision-making, intended that most decisions be made by the supervising judge. This supports the view that those decisions should be interfered with only in clear cases.

- 29 The standard of review of this Court, in reviewing the CCAA decision of the supervising judge, is therefore one of correctness if there is an error of law. Otherwise, for an appellate court to interfere with the decision of the supervising judge, there must be a palpable and overriding error in the exercise of discretion or in findings of fact.

Statutory Provisions

- 30 The CCAA includes provisions defining secured creditor, unsecured creditor, refers to classes of them, and provides for court approval of a plan of compromise or arrangement in the following sections:

2. Interpretation

.....

"secured creditor" means a holder of a mortgage, hypothec, pledge, charge, lien or privilege on or against, or any assignment, cession or transfer of, all or any property of a debtor company as security for indebtedness of the debtor company, or a holder of any bond of a debtor company secured by a mortgage, hypothec, pledge, charge, lien or privilege on or against, or any assignment, cession or transfer of, or a trust in respect of, all or any property

of the debtor company, whether the holder or beneficiary is resident or domiciled within or outside Canada, and a trustee under any trust deed or other instrument securing any of those bonds shall be deemed to be a secured creditor for all purposes of this Act except for the purpose of voting at a creditors' meeting in respect of any of those bonds;

.....

"Unsecured creditor" means any creditor of a company who is not a secured creditor, whether resident or domiciled within or outside Canada, and a trustee for the holders of any unsecured bonds issue under a trust deed or other instrument running in favour of the trustee shall be deemed to be an unsecured creditor for all purposes of this Act except for the purpose of voting at a creditors' meeting in respect of any of those bonds.

Compromises and Arrangements

4. Where a compromise or an arrangement is proposed between a debtor company and its unsecured creditors or any class of them, the court may, on the application in a summary way of the company, of any such creditor or of the trustee in bankruptcy or liquidator of the company, order a meeting of the creditors or class of creditors, and, if the court so determines, of the shareholders of the company, to be summoned in such a manner as the court directs.

5. Where a compromise or an arrangement is proposed between a debtor company and its secured creditors or any class of them, the court may, on the application in a summary way of the company or of any such creditor or of the trustee in bankruptcy or liquidator of the company, order a meeting of the creditors or class of creditors, and, if the court so determines, of the shareholders of the company, to be summoned in such manner as the courts directs.

.....

6. Where a majority in number representing two-thirds in value of the creditors, or class of creditors, as the case may be, present and voting either in person or by proxy at the meeting or meetings thereof respectively held pursuant to sections 4 and 5, or either of those sections, agree to any compromise or arrangement either as proposed or as altered or modified at the meeting or meetings, the compromise or arrangement may be sanctioned by the court, and if so sanctioned is binding

(a) on all the creditors or the class of creditors, as the case may be, and on any trustee for any such class of creditors, whether secured or unsecured, as the case may be, and on the company; and

(b) in the case of a company that has made an authorized assignment or against which a receiving order has been made under the *Bankruptcy and Insolvency Act* or is in the course of being wound up under the *Winding-up and Restructuring Act*, on the trustee in bankruptcy or liquidator and contributories of the company.

Classes of Creditors

- 31 It is apparent from a review of the foregoing sections that division into classes of creditors within the unsecured and secured categories may, in any given case, materially affect the outcome of the vote referenced in section 6. Compliance with section 6 triggers the ability of the court to approve or sanction the Plan and to bind the parties referenced in s. 6(a) and 6(b) of the CCAA. In argument before me, it was conceded by the applicant that Resurgence would not have the ability to ensure approval of the Plan by casting its vote if Air Canada were to be excised from the unsecured creditor category into a separate class. Conversely, counsel for Resurgence candidly admitted that Resurgence would effectively have a veto of the Plan if Air Canada were segregated into a separate class of unsecured creditor.

Application of the Criteria for Leave to Appeal

- 32 The four elements of the general criterion are set out in paragraph [7]. The first and second elements are satisfied in this case. The points raised on appeal are of significance to the action. If Resurgence succeeds, it obtains a veto. If it does not succeed, and it votes as a member of the unsecured creditors class with Air Canada, Air Canada can control the vote of the unsecured creditors.
- 33 In terms of the points on appeal being of significance to the practice, it may be that an appellate court's views in this province on the classification of unsecured creditors issue is desirable, there being no appellate authority from this Court on this issue. Although I have doubt as to the significance of this element of the general criterion in the context of the facts of this case, I am prepared for the purposes of this application to treat this element as having being satisfied.
- 34 The third element is whether the appeal is *prima facie* meritorious or, on the other hand, whether it is frivolous. In my view, the proper interpretation of this element is not a mutually exclusive application of an appeal being either meritorious or frivolous. Rather, the appeal must be *prima facie* meritorious; if it is not *prima facie* meritorious, this element is not satisfied.
- 35 I find that the appeal on the points raised from the Decision is not *prima facie* meritorious. In the plain ordinary meaning of the words of this element, on first impression, there must appear to be an error in principle of law or a palpable and overriding error of fact. Exercise of discretion by a supervising judge, so long as it is exercised judicially, is not a matter for interference by an appellate court, even if the appellate court were inclined to decide the matter another way. It is precisely this kind of a factor which breathes life into the modifier "*prima facie*" meritorious.
- 36 I have carefully reviewed all of the cases referred to by the supervising chambers judge and the principles she derived from them. In my view, she made no error in law.

- 37 In the exercise of her discretion, she decided neither to allow the applicant's motion to excise Air Canada from the unsecured creditors class nor to prohibit Air Canada from voting. She also declined, on the facts established before her, to separate creditors of CAC from creditors of CAIL for voting purposes. She did, however, order that Air Canada's vote be recorded and tabulated and indicated that this will be considered at the Fairness Hearing.
- 38 It was strenuously argued before me by the applicant, that deferring classification and voting issues to the Fairness Hearing was an error of law or principle in and of itself.
- 39 The argument was put in terms that if, on a proper classification of unsecured creditors, Air Canada was removed from the unsecured class, and Resurgence vetoed the Plan, the matter of a Fairness Hearing would never arise. While that may be true, it does not follow that there is any error in law in what the supervising judge did. She concluded that the separate tabulation of the votes will allow the voice of the unsecured creditors to be heard, while, at the same time, permit, rather than rule out the possibility, that the Plan might proceed. This approach is consistent with the purpose of the CCAA as articulated in many of the authorities in this country.
- 40 The supervising chambers judge also refused to exclude Air Canada from voting on the basis that the legal rights attached to the notes held by Air Canada were valid. Resurgence argued that because Air Canada had other interests in the outcome of the Plan, it should be excluded from voting as an unsegregated secured creditor. Paperny, J. held that this was an issue of fairness, as was the fact that Air Canada was really voting on its own reorganization. She did not err in principle. She expressly acknowledged the authorities that, on different facts, either allowed different classes or excluded a vote. See, for example, *Re Woodward's Ltd.* (1993), 84 B.C.L.R. (2d) 206 (B.C. S.C.); *Re Northland Properties Ltd.* (1988), 73 C.B.R. (N.S.) 166 (B.C. S.C.); *Re NsC Diesel Power Inc.* (1990), 79 C.B.R. (N.S.) 1 (N.S. T.D.).
- 41 The fourth element of the general criterion is whether the appeal will unduly hinder the progress of the action. In other words, will the delay involved in prosecuting, hearing and deciding the appeal be of such length so as to unduly impede the ultimate resolution of the matter by a vote or court sanction? The approach of the supervising judge to the issues raised by the applicant is that its concerns will be seriously addressed at the Fairness Hearing scheduled for June 5, 2000, pursuant to s.6 of the CCAA, provided the creditors vote to adopt the Plan.
- 42 This element has at its root the purpose of the CCAA; the role of the supervising judge; the need for a timely and orderly resolution of the matter; and the effect on the interests of all parties pending a decision on appeal. The comments of McFarlane, J.A. in *Re Pacific National Lease Holding Corp.* (1992), 15

C.B.R. (3d) 265 (B.C. C.A. [In Chambers]) are particularly apt where he stated as follows at p.272:

Despite what I have said, there may be an arguable case for the petitioners to present to a panel of this Court on discreet questions of law. But I am of the view that this Court should exercise its powers sparingly when it is asked to intervene with respect to questions which arise under the C.C.A.A. The process of management which the Act has assigned to the trial Court is an ongoing one. In this case a number of orders have been made. Some, including the one under appeal, have not been settled or entered. Other applications are pending. The process contemplated by the Act is continuing.

A colleague has suggested that a judge exercising a supervisory function under the C.C.A.A. is more like a judge hearing a trial, who makes orders in the course of that trial, than a chambers judge who makes interlocutory or proceedings for which he has no further responsibility.

Also, we know that in a case where a judgment has not been entered, it may be open to a judge to reconsider his or her judgment, and alter its terms. In supervising a proceeding under the C.C.A.A. orders are made, and orders are varied as changing circumstances require. Orders depend upon a careful and delicate balancing of a variety of interests and of problems. In that context appellate proceedings may well upset the balance, and delay or frustrate the process under the C.C.A.A. I do not say that leave will never be granted in a C.C.A.A. proceeding. But the effect upon all parties concerned will be an important consideration in deciding whether leave ought to be granted.

- 43 In that case, it appears that McFarlane, J.A. was satisfied that the first three elements of the criteria had been met, i.e. that there "may be an arguable case for the petitioners to present to a panel of this court on discrete [sic] questions of law".
- 44 It was argued before me that an appeal would give rise to an uncertainty of process and a lack of confidence in it; that the creditors, or some of them, may be inclined to withdraw support for the Plan that would otherwise be forthcoming, but for the delay. None of the parties tendered affidavit evidence on this issue.
- 45 Nowhere in any of the authorities has the issue of onus in meeting the elements the general criterion been prominent. I am of the view that the onus is on the applicant. That onus would include the applicant producing at least some evidence on the fourth element to shift the onus to the respondents, even though it involves proving a negative, i.e. that there will not be any material adverse impact as the result of the delay occasioned by an appeal. That evidence is lacking in this case. It is lacking on both sides but the respondents do not have an initial onus in this regard. Therefore, I find that the fourth element has not been established by the applicant.
- 46 The last step in a proper analysis in the context of a leave application is to ascribe appropriate weight to each of the elements of the general criterion and

decide over all whether the test has been met. In most cases, the last two elements will be more important, and ought to be ascribed more weight than the first two elements. The last two elements here have not been met while the first two arguably have. In the result, I am satisfied that the applicant has not met the threshold for leave to appeal on the basis of the authorities, and I am therefore denying the application.

Conclusion

- 47 The application for leave to appeal the Decision is dismissed on the basis that there is no *prima facie* meritorious case and that the granting of leave would likely unduly hinder the progress of the action.

Application dismissed.

TAB 2

**In The Matter Of The Companies'
Creditors Arrangement Act, R.S.C.
1985, c. C-36, As Amended;**

**And In The Matter Of The Courts
of Justice Act, R.S.O. 1990, c. C-43,
as amended;**

**And In The Matter Of A Plan of
Compromise or Arrangement of Country
Style Food Services Inc., Country Style
Food Services Holdings Inc., Country Style
Realty Limited, Melody Farms Specialty
Foods and Equipment Limited, Buns
Master Bakery Systems Inc. and Buns
Master Bakery Realty Inc.;**

**Application Under the Companies'
Creditors Arrangement Act, R.S.C.
1985, c. C-36
(M28458)**

**Indexed As: Country Style Food Services
Inc. et al., Re**

**Ontario Court of Appeal
Feldman, J.A.
April 16, 2002.**

Summary:

A motions judge sanctioned a plan of arrangement under the Companies' Creditors Arrangement Act for the respondent, Country Style Group of Corporations (a franchise). Three Country Style franchisees sought leave to appeal the order.

The Ontario Court of Appeal, per Feldman, J.A., dismissed the application.

Creditors and Debtors - Topic 8599

Debtors' relief legislation - Companies' creditors arrangement legislation - Appeals

(incl. leave to appeal) - A motions judge sanctioned a plan of arrangement under the Companies' Creditors Arrangement Act for the Country Style Group of Corporations (a franchise) - Three Country Style franchisees sought leave to appeal the order - They argued that some franchisees over-contributed to a national advertising fund in relation to other franchisees entitling them to make a claim against the company for unjust enrichment - However, because they did not know about this potential claim until after the sanction hearing, they did not file claims in the process, participate as unsecured creditors, and have the right to vote for or against the plan - The Ontario Court of Appeal, per Feldman, J.A., dismissed the application - There was nothing to suggest that the plan as sanctioned and approved by the court was not "fair and reasonable" - If leave to appeal was granted, the progress of the action would be hindered and the restructuring might not go ahead at all - The applicants did not propose any alternative to the plan - The significance to the action appeared to be procedural but not substantive - See paragraphs 15 to 20.

Cases Noticed:

R. v. Palmer, [1980] 1 S.C.R. 759; 30 N.R. 181, refd to. [para. 4].

Consumers Packaging Inc., Re (2001), 150 O.A.C. 384; 27 C.B.R.(4th) 197 (C.A.), refd to. [para. 15].

Blue Range Resources Corp., Re (1999), 244 A.R. 103; 209 W.A.C. 103; 12 C.B.R.(4th) 186 (C.A.), refd to. [para. 15].

Multitech Warehouse Direct Inc., Re (1995), 32 Alta. L.R.(3d) 62 (C.A.), refd to. [para. 15].

Cineplex Odeon Corp. (2001), 24 C.B.R.

(4th) 201 (Ont. C.A.), reld to. [para. 15].

Counsel:

Craig R. Colrairie and Mitchell D. Goldberg, for Tozeng Ltd., 1124019 Ontario Ltd. and 665371 Ontario Ltd., applicants; Joanna Board, for 1304271 Ontario Ltd. and 995804 Ontario Inc. (supporting the applicants);

Patrick J. O'Kelly and Ashley J. Taylor, for Country Style, respondent;

Frank J.C. Newbould, Q.C., for the Bank of Nova Scotia, respondent;

Mahesh Uttamchandani, for CAI, DIP Lender, respondent.

This application was heard on April 15, 2002, before Feldman, J.A., of the Ontario Court of Appeal, who released the following decision on April 16, 2002.

[1] **Feldman, J.A. [in Chambers]:** This is an application for leave to appeal the order of Spence, J., made on March 7, 2002, whereby he sanctioned a Plan of Arrangement (the "Plan" under the **Companies' Creditors Arrangement Act**, R.S.C. 1985, c. C-36 ("CCAA") for the respondent, Country Style Group of Corporations. The application is brought under s. 13 of the CCAA which provides:

"s. 13 Except in the Yukon Territory, any person dissatisfied with an order or a decision made under this Act may appeal therefrom on obtaining leave of the judge appealed from or of the court or a judge of the court to which the appeal lies and on such terms as to security and in other respects as the judge or court directs:"

[2] The application was originally brought

before Spence, J., but as he was unable to hear it before April 16, 2002, the date scheduled for the closing of the plan transaction, he suggested that the application be brought to this court.

[3] All three applicants are Country Style franchisees. Only one, Tozeng Limited, is also a creditor that filed a proof of claim and voted in the proceeding.

[4] The applicants concede that on the record before him, Spence, J., did not make any error in approving the Plan which was approved by a substantial percentage of the unsecured creditors and by the secured creditor. In fact, no one opposed the approval of the plan at the sanction hearing. The basis for this application is that immediately after the hearing approving the Plan, the applicants became aware of facts which they say vitiate the approval process in three ways:

(1) Over a period of time, some franchisees had contributed to Country Style's national advertising fund while others had not. The applicants claim that to the extent that some franchisees thereby over-contributed, they were entitled to claim as creditors against the company for unjust enrichment in the Plan process. However, because they did not know about the over-contribution and unequal treatment until it was too late to claim in the plan process, they have been denied both the amount of their claim and the opportunity to vote for or against the Plan and to participate in the process.

(2) The company was offering improper incentives to creditors to vote for the Plan.

(3) The Monitor was in a conflict of interest.

The applicants rely on fresh evidence in order to assert these claims and rely on s. 134(4) of the **Courts of Justice Act**, R.S.O. 1990, c. C-43, which allows a court in a proper case, to accept fresh evidence. In **R. v. Palmer**, [1980] 1 S.C.R. 759; 30 N.R. 181, at 775, the Supreme Court of Canada set out four criteria for the admission of fresh evidence on appeal, summarized as follows:

(1) by due diligence, the evidence could not have been adduced in the proceeding below;

(2) it is relevant to a decisive or potentially decisive issue;

(3) it is reasonably capable of belief;

(4) if believed, it may reasonably have affected the result.

[5] The respondents object to the admission of the fresh evidence on this application and rely heavily on the assertion that the first criterion, due diligence, has not been met in this case. They also suggest that the record discloses that Mr. English, the principal of Tozeng Limited, did know about the differential treatment of franchisees as long as one year ago.

[6] Mr. O'Kelly on behalf of Country Style, points to the fact that a creditor, Tarragon Mercantile Inc., did propose to oppose the sanction order until an out-of-court settlement was reached on the evening before the sanction motion. Tarragon filed a motion record with the court that contained af-

fidavits outlining some of the allegations on which the applicants now rely (in particular, the alleged irregularities with the proxy solicitation process and the alleged conflict of interest of the Monitor) and raised other matters as well. I am told that Spence, J., was advised on the return of the motion that Tarragon was withdrawing its opposition. The plan was thereupon sanctioned by the court. I am advised that no one opposed the order.

[7] Mr. O'Kelly's submission is that because Tarragon was in a position to find out the information necessary to bring forth some of the allegations now asserted by the applicants, the applicants could have done so as well had they exercised due diligence. In my view, on the face of it, there is merit in that submission.

[8] The one issue which is not fully detailed in the Tarragon material is the national advertising fund issue. However, the information relied on in respect of the fund is contained in an affidavit of Catherine Mauro dated March 25, 2002 and filed on this application. She is the former director of marketing and product development who was terminated by Country Style on February 4, 2002. Ms Mauro also provided one of the affidavits which is included in the Tarragon material. Again, therefore, it appears that the applicants could have discovered further information from Ms. Mauro prior to the March 7 hearing had they acted with due diligence in speaking with her.

[9] Even more significant, however, is the fact that in his affidavit filed in connection with the original material seeking court protection, Mr. Gibbons, the President of Country Style, disclosed as part of his de-

scription of the financial status of the debtor companies that one of the historical responses by management when a franchisee developed financial difficulties was "deferring or accepting reduced royalty, advertising and/or sign rental payments for a period of time" (affidavit para. 37). This information was also included in the Management proxy circular which was sent out to all creditors, of which Mr. English was one.

[10] The applicants' position is that until they talked to Catherine Mauro after the sanction hearing, they did not know that some franchisees were not paying the full 3.5% of monthly gross sales to the national advertising fund, and that the 13 corporate stores, taken over from failed franchisees, paid nothing into the fund. The applicants also take the position that the company and the monitor made it impossible for the franchisees to learn of this by failing to disclose it to the franchisees. Their evidence is that representations were made to franchisees by senior management that all franchisees paid the same percentage of their sales into the national advertising fund.

[11] However, it appears that there was disclosure of the differential treatment of franchisees in respect of the advertising fund in Mr. Gibbons' affidavit and the Management circular. Counsel also pointed out that franchisees could ask to be added to the service list for all of the documentation and that some were added, including Ms. Board's clients who have been represented by her here in support of the application.

[12] I conclude, based on the material currently before the court, that it cannot be said that there was non-disclosure of the differen-

tial treatment of franchisees in respect of the contribution to the national advertising fund, or that the applicants could not have discovered this evidence if they had exercised due diligence. Although it appears that the potential significance of the different contributions as a possible claim against Country Style based on unjust enrichment, may not have been considered by the applicants until after the sanction motion, a failure to appreciate the significance of information does not meet the due diligence test.

[13] Finally, the respondents point to the fact that Mr. English has deposed that in May 2000, he sought and obtained differential treatment in respect of the royalty fees he was paying and that he has been trying to retain the so-called "tiered store" status for his stores which allows them to pay lower fees. Therefore, Mr. English was aware of differentiation among franchisees in respect of some of the amounts payable to the franchiser and wanted to preserve that differentiation when it benefited him. The respondents say this shows that the new evidence should not be accepted and that furthermore, there is no merit to the suggestion that the franchisees have any claim against the debtor company based on alleged overpayments. As a result, they argue that the new evidence would not have affected the outcome of the sanction hearing had it been available at that hearing.

[14] I am satisfied that I need not deal with this part of the submission on this motion, as the due diligence criterion is not met.

[15] Even if the fresh evidence met the test for admission, which it does not on the due diligence criterion, the court must be satisfied that this is a case where leave to appeal

ought to be granted. The jurisprudence in this area dictates that leave to appeal in CCAA proceedings should be granted sparingly: **Consumers Packaging Inc., Re** (2001), 150 O.A.C. 384; 27 C.B.R. (4th) 197, at 199 (C.A.); **Blue Range Resources Corp., Re** (1999), 244 A.R. 103; 209 W.A.C. 103; 12 C.B.R. (4th) 186, at 190 (C.A.). In order to grant leave the court must be satisfied that there are "serious and arguable grounds that are of real and significant interest to the parties": **Multitech Warehouse Direct Inc., Re** (1995), 32 Alta. L.R. (3d) 62, at 63 (C.A.). This is determined in accordance with a four-pronged test as follows:

- (a) whether the point on appeal is of significance to the practice;
- (b) whether the point is of significance to the action;
- (c) whether the appeal is prima facie meritorious or frivolous;
- (d) whether the appeal will unduly hinder the progress of the action.

See **Blue Range Resource Corp.**, supra, at 190; **Cineplex Odeon Corp.** (2001), 24 C.B.R. (4th) 201, at 202 (Ont. C.A.).

[16] As I understand it, the main issue on appeal is the submission that the applicant franchisees and other franchisees, some of whom have filed affidavits in support, overcontributed to the national advertising fund in relation to other franchisees and the company in connection with its corporate stores. This overcontribution entitled them to make a claim against the company for unjust enrichment. However, because they did not

know about this potential claim until after the sanction hearing, they did not file claims in the process; they therefore did not have the right to participate as unsecured creditors, and they did not have the right to vote for or against the Plan.

[17] Counsel for the applicants concedes that there is no evidence in the record to demonstrate that had the affected franchisees made claims and voted, the Plan would have been defeated or amended in any way.

[18] Counsel also concedes that no alternative plan has been proffered at any stage. He suggests, however, that because of the circumstances set out, the Plan cannot be considered fair and reasonable. The Monitor has made it clear in its reports that the only alternative to the Plan is bankruptcy or receivership, whereunder there would be nothing for the unsecured creditors. Counsel suggested in argument that his clients would be prepared to see the debtor company go bankrupt rather than proceed with the sanctioned Plan. There is no affidavit evidence to this effect, and I frankly find it hard to accept that franchisees with viable operations would prefer to see the corporate entity with which they are associated be liquidated in a bankruptcy or receivership.

[19] Based on the record, there is nothing to suggest that the Plan as sanctioned and approved by the court is not "fair and reasonable." If leave to appeal is granted, the progress of the action will clearly be hindered and the restructuring may not go ahead at all. If the appeal were to be successful and the process reopened, the applicants do not propose any alternative to the plan, so that the significance to the action appears to be procedural but not substantive.

[20] For all of these reasons, the applicants have not satisfied the test for the court to exercise its discretion to grant leave to appeal.

[21] During argument, counsel for the applicants suggested that one of the problems facing his clients is that they owe money to the debtor company, but are not able to make a claim against the company in respect of the overpayment into the advertising fund because of the orders made in the CCAA process. In response, counsel for Country Style took the position that s. 18.1 of the CCAA preserves the applicants' ability to assert a right of set-off against the company in respect of their claims against any monies which they may owe to the company. In other words, their claims against the company are not necessarily barred.

[22] As this was not an issue for resolution on this leave to appeal motion, I make no comment on (1) the effect of s. 18.1 of the CCAA on post-Plan claims by or against the debtor company; or (2) on the effect of the claims bar order in respect of claims by people who were not listed or served as creditors in the proceeding, or people who did not know that they had claims against the company.

[23] Finally, I note that the franchisees as a group were not considered to be people to be officially served with and included in the CCAA process. I was advised by a representative of the Monitor who was present in court for this appeal, that Mr. Gibbons did send a letter to all franchisees enclosing the original stay order and advising them of the Monitor's website where much of the CCAA material would be posted. Although the process under the Act contemplates the

participation and protection of creditors, the debtor company, and possibly the shareholders, in cases where the debtor company is a franchisor, the franchisees may have an interest in the ultimate structure of the franchise operation as proposed by the Plan process. It may therefore be appropriate where a franchisor seeks CCAA protection, to consider whether the franchisees ought to be given notice of the proceedings and the opportunity to request the ability to participate on an appropriate basis.

CONCLUSION

[24] Leave to appeal is denied.

Application dismissed.

Editor: Rodney A. Jordan/gs

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

Court of Appeal File No. M38120

AND IN THE MATTER OF a Plan of Compromise or Arrangement of Grant Forest Products Inc.,
Granter Alberta Inc., Grant Forest Products Sales Inc. and Grant U.S. Holdings GP

COURT OF APPEAL FOR ONTARIO

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