Court File No. CV-09-8247-00CL

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 GRANT FOREST PRODUCTS INC., GRANT ALBERTA INC., GRANT FOREST PRODUCTS SALES INC. and GRANT U.S. HOLDINGS GP (the "Applicants")

BRIEF OF AUTHORITIES
(Motion returnable August 6, 2009)

August 4, 2009

FRASER MILNER CASGRAIN LLP
100 King Street West
1 First Canadian Place
Toronto, Ontario
M5X 1B2

Daniel R. Dowdall
LSUC No. 16737D
Telephone: 416 863-4700
E-Mail: daniel.dowdall@fmc-law.com

Jane O. Dietrich
LSUC No. 49302U
Telephone: 416 863-4467
E-Mail: jane.dietrich@fmc-law.com

Lawyers for the Applicants Grant Forest Products Inc., Grant Alberta Inc., Grant Forest Products Sales Inc., and Grant U.S. Holdings GP

TO: SERVICE LIST

Index

TAB 1

HMANALY N§79

Houlden and Morawetz Bankruptcy and Insolvency Analysis

L.W. Houlden and Geoffrey B. Morawetz

Companies' Creditors Arrangement Act
Sections 11-11.11
N§79 — Key Employee Retention Plans and Key Employee Incentive Plans

N§79 — Key Employee Retention Plans and Key Employee Incentive Plans

See s. 11.11

In some instances, the court supervising the *CCAA* proceeding will authorize a key employee retention plan or key employee incentive plan. Such plans are aimed at retaining employees that are important to the management or operations of the debtor company in order to keep their skills within the company at a time when they are likely to look for other employment because of the company's financial distress.

A debtor company sought a new priority charge on its assets for an employee retention program, aimed at ensuring the retention of all its current employees until the end of the *CCAA* process, a part of the amount to be paid only in the event that a plan is approved by creditors and sanctioned by the court and part to be paid regardless of the outcome. The Court held that for purposes of determining whether to grant a priority charge, it accepted the proposition that the Employee Retention Charge was no different than a DIP financing priority charge in that it was aimed at allowing the debtor to continue operating. It held that there is now authority for approving DIP financing on a priority basis in Québec. However, on the facts of the case, the Court did not exercise its jurisdiction to allow creation of the Employee Retention Charge because: 1) it was not persuaded that the debtor had established that there was a reasonable prospect of the successful restructuring; 2) the balance that must exist between interest and prejudice amongst creditors did not appear to be present; and 3) the salary increase claims of employees would be better protected than the claims of those no longer employed, which did not appear to be just and equitable. The Court held that if the Employee Retention Charge was indeed key to the restructuring, it was difficult to understand why the charge was to be created only at the expense of the unsecured creditors and not the secured creditors, given that the secured creditors would benefit from a successful restructuring without sharing in the cost in any manner: *Re MEI Computer Technology Group Inc.* (2005), 2005 CarswellQue 3675, [2005] R.J.Q. 1558, REJB 2005-90239, 19 C.B.R. (5th) 257 (Que. S.C.).

At the time of filing a *CCAA* proceeding, the chief financial officer (CFO) of the debtor had obtained alternative employment but was persuaded by principals to stay, with an agreement for payment of a termination lodged with the debtor's solicitors. The letter specified that the agreement was subject to approval of the senior secured creditor, but it received no notice nor was approval sought. The CFO brought a motion for determination that he was entitled to the amount, and the secured creditor objected. The court granted the motion, finding that it was reasonable to infer that had the issue of the termination agreement been included in a report to the court soon after appointment of the monitor, it would likely have been approved. The senior unsecured creditor approved of the payment, and the termination amount was only payable if the CFO remained employed and the restructuring process turned into a realization process, which is what occurred. The court held that the termination agreement was intended to and did meet the requirements for retention bonus as provided for in the initial order; the agreement was entered into on a *bona fide* basis within the terms of the initial order; and the CFO was entitled to the money: *Re Warehouse Drug Store Ltd.* (2006), 2006 CarswellOnt 5128, 24 C.B.R. (5th) 275 (Ont. S.C.J.).

The court approved a key employee retention program under *CCAA* proceedings, having regard for the fact that a similar order was being sought from the U.S. bankruptcy court with carriage of concurrent Chapter 11 proceedings. The court relied in part on the protocol that it had endorsed, which was expected to be endorsed by the U.S. court: *Re Quebecor World Inc.* (2008), 2008 CarswellQue 3018, 45 C.B.R. (5th) 114 (Que. Bktcy.).

The Ontario Superior Court of Justice granted orders approving a key employee incentive plan (KEIP) and a key employee retention plan (KERP). The monitor reported that the plans had been developed to incent employees who were absolutely key to the success of the restructuring to remain with the Canadian and U.S. debtors through to the completion of the proceedings. Justice Morawetz was satisfied that the employees were sought after by competitors, even given current market conditions. In designing the plans, the debtor obtained independent advice that included benchmarking total direct compensation levels against industry standards in comparing other key employee incentive plans approved recently by the courts. The eligible employees represented 5 percent of the debtor's global workforce. The potential dollar value to be paid out under the KERP was approximately $22 million of which $6.2 million was allocated to the Canadian applicants. The awards under both the KEIP and the KERP would vest based on the achievement of three milestones: namely, achievement of North American objectives; achievement of certain parameters that would result in a more focused organization; and court-approved confirmation of the plan of restructuring: *Re Nortel Networks Corp.* (2009), 2009 CarswellOnt 1330 (Ont. S.C.J. [Commercial List]).

END OF DOCUMENT

TAB 2

[2005] R.J.Q. 1558, EYB 2005-90239, J.E. 2005-1009, 19 C.B.R. (5th) 257

2005 CarswellQue 3675

MEI Computer Technology Group Inc., Re
In the matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended: MEI Computer Technology Group Inc. (Petitioner) and Ernst & Young Inc. (Monitor)
Quebec Superior Court
Gascon S.C.J.
Heard: April 29, 2005
Judgment: May 6, 2005
Docket: C.S. Montréal 500-11-025430-055

Counsel: Me Alain Tardif, Me Miguel Bourbonnais for Petitioner

Subject: Insolvency; Labour and Employment; Public

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

Creation of priority charge -- Corporation under protection of Companies' Creditors Arrangement Act applied for creation of new priority charge on assets, ranking prior to unsecured creditors, for amount of key employee retention programme -- Programme provided that amount covered by charge would be paid regardless of restructuring's outcome -- Application dismissed -- Charge sought was comparable to DIP financing to allow debtor corporation to continue operating -- Review of case law and doctrine on issue of courts' exercise of their inherent jurisdiction to grant DIP financing or priority charges revealed following guidelines: DIP financing or priority charge is extraordinary measure that should be used sparingly and in clear cases; evidence should show that benefits to all parties clearly outweigh potential prejudice to some creditors; charge must be critical to continue operating business and successful restructuring; charge must be urgent need; reasonable prospect of successful restructuring must exist; charge should be available only in limited amounts and for brief period; charge must be just and equitable in circumstances to warrant exercise of inherent jurisdiction powers to order charge -- Facts of case did not support exercise of inherent jurisdiction to create employee retention charge -- Amount covered by charge would be paid regardless of outcome of CCAA restructuring -- Charge would finance "salary increase" for remaining employees by corporation's unsecured creditors, including employees who lost jobs -- Charge would create imbalance in same class of creditors as other unsecured creditors were likely to be paid far less than 100 per cent of outstanding claims -- Charge would be at sole expense of unsecured creditors; secured creditors would not share in burden -- Corporation's cash flow was not insufficient to assure payment of remaining employees -- This was not clear case of urgency requiring creation of charge to continue operating business -- Lack of opposition to application was not good enough reason to be lenient where recognized criteria for granting priority charges were not met.

Faillite et insolvabilité --- Proposition -- Loi sur les arrangements avec les créanciers des compagnies -- Questions diverses

Création d'une priorité -- Compagnie sous la protection de la Loi sur les arrangements avec les créanciers des compagnies a demandé la création d'une nouvelle priorité sur les biens prenant rang avant les créanciers non garantis pour un montant prévu par un programme de rétention des employés clés -- Programme prévoyait que le montant couvert par la priorité serait payé peu importe l'issue de la restructuration -- Demande rejetée -- Priorité demandée était similaire au financement FDE accordé à une compagnie débitrice pour lui permettre de continuer -- Revue de la jurisprudence et de la doctrine portant sur l'exercice par le tribunal d'exercer sa compétence inhérente pour accorder un financement FDE ou des priorités a révélé les critères suivants: financement FDE ou priorité est une mesure extraordinaire qui doit être utilisée avec modération et dans les cas clairs; preuve doit établir que les avantages pour toutes les parties l'emportent clairement sur le préjudice éventuel pour certains créanciers; priorité doit être essentielle à l'exploitation de l'enterprise et à la réussite de la restructuration; priorité doit être un besoin urgent; il faut une perspective raisonnable de réussir la restructuration; priorité ne devrait être accordée que pour des montants limités et pour une courte période; priorité doit être juste et équitable dans les circonstances pour justifier d'exercer la compétence inhérente pour l'accorder -- Faits de l'affaire ne justifiait pas la création d'une priorité pour la rétention des employés -- Montant couvert par la priorité serait payé peu importe l'issue de la restructuration sous la LACC -- Priorité ferait que les créanciers non garantis de la compagnie, y compris les employés sans emploi, financerait une "augmentation de salaire" pour les employés restants -- Priorité créerait un déséquilibre au sein d'un même groupe de créanciers, puisque les autres créanciers non garantis recevraient probablement beaucoup moins que 100 pour cent des réclamations impayées -- Priorité ne serait faite qu'aux dépens des créanciers non garantis; les créanciers garantis ne supporteraient pas le fardeau -- Liquidités de la compagnie n'étaient pas insuffisantes pour assurer le paiement des employés restants -- Il ne s'agissait pas d'un cas clair d'urgence requérant la création d'une priorité pour continuer d'exploiter l'entreprise -- Absence d'opposition à la demande n'était pas une assez bonne raison pour être indulgent alors que les critères reconnus pour accorder une priorité n'ont pas été remplis.

Cases considered by Gascon S.C.J.:

Air Canada, Re (2003), 2003 CarswellOnt 1220 (Ont. S.C.J. [Commercial List]) -- referred to

Dylex Ltd., Re (1995), 31 C.B.R. (3d) 106, 1995 CarswellOnt 54 (Ont. Gen. Div. [Commercial List]) -- referred to

Hunters Trailer & Marine Ltd., Re (2001), 2001 CarswellAlta 964, [2001] 9 W.W.R. 299, 27 C.B.R. (4th) 236, 94 Alta. L.R. (3d) 389, 2001 ABQB 546, 295 A.R. 113 (Alta. Q.B.) -- referred to

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

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

PCI Chemicals Canada Inc., Re (2002), 2002 CarswellQue 831, [2002] R.J.Q. 1093 (Que. S.C.) -- considered

Royal Oak Mines Inc., Re (1999), 1999 CarswellOnt 792, 7 C.B.R. (4th) 293 (Ont. Gen. Div. [Commercial List]) -- referred to

Stelco Inc., Re (2005), 253 D.L.R. (4th) 109, 75 O.R. (3d) 5, 2005 CarswellOnt 1188, 2 B.L.R. (4th) 238, 9 C.B.R. (5th) 135, 196 O.A.C. 142 (Ont. C.A.) -- considered

Sulphur Corp. of Canada Ltd., Re (2002), 2002 ABQB 682, 2002 CarswellAlta 896, 35 C.B.R. (4th) 304, [2002] 10 W.W.R. 491, 5 Alta. L.R. (4th) 251, 319 A.R. 152 (Alta. Q.B.) -- referred to

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

Westar Mining Ltd., Re (1992), 14 C.B.R. (3d) 95, 1992 CarswellBC 509 (B.C. S.C.) -- considered

Statutes considered:

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

Generally -- considered

s. 11 -- referred to

APPLICATION for creation of priority charge for employee retention programme on assets of corporation under protection of Companies' Creditors Arrangement Act.

***Gascon S.C.J.*:**

1 In the context of an Amended Motion for the First Extension of the Initial Order issued under the CCAA[FN1], MEI Computer Technology Group Inc. (MEI) requests the creation of a new priority charge on its assets, namely what it calls an Employee Retention Charge.

2 In the Initial Order, the Court already authorized the creation of a Directors and Officers Indemnification Charge, for an aggregate amount of $300,000, as well as the creation of an Administration Charge for the Monitor, its legal counsel, MEI's legal counsel and other advisers, for a further amount of $200,000.

3 The Administration Charge ranks prior to all security on MEI's assets, while the D&O charge ranks prior to all such security with the exception of the Administration Charge and the security held by the National Bank of Canada.

4 The Employee Retention Charge that MEI now wants this Court to order pertains to an Employee Retention Programme being presently contemplated by the company[FN2].

5 The Programme is aimed at ensuring the retention of all current employees until the end of the *CCAA* process, and thus sets targets for each of them in furtherance of a successful restructuring. The total value of the Programme is as much as $455,000 based on performance. Fifty-three (53) employees divided in four (4) groups (General, Project managers and key analysts, Management, and Chief restructuring officer) are covered by the

Programme.

6 A first portion of the Programme relates to specific targets to be reached for a potential total amount of $265,000. These target amounts are only payable in the event that a Plan is approved by the creditors and sanctioned by the Court at the end of the *CCAA* process. In such instance, it is expected that the Plan will provide for the payment of these target amounts in full prior to the mass of unsecured claims. However, these target amounts are not in themselves secured.

7 A second portion of the Programme represents base amounts totalling $190,000 that will be paid to all employees covered by the Programme who are still with MEI at the conclusion of the *CCAA* proceedings. The Programme provides for the payment of that second portion regardless of the outcome of the restructuring.

8 The charge that MEI requests concerns solely the base amounts of the Programme. MEI wants the Court to create a charge to guarantee the payment of these amounts totalling $190,000 in order not to compromise the company's cash flow. It asks that the charge ranks immediately after all existing security on MEI's assets, but prior to all subsequent security, and obviously prior to all the unsecured creditors.

9 As appears from the Initial Order, the secured creditors' claims aggregate $1,490,000, while the two priority charges created at that time amount to another $500,000. Therefore, the existing security on MEI's assets stand at $1,990,000.

10 In comparison, the unsecured claims aggregate approximately $3,677,000. They include the claims of trade creditors for $710,000, employees' claims in accrued vacation pay, unpaid severance or unpaid commissions for $1,467,000, and two contingent claims against which MEI acknowledged an indebtedness totalling $1,500,000.

11 MEI argues that the creation of the Employee Retention Charge is needed for the restructuring process. Since the beginning of the *CCAA* application, it says that twenty-seven (27) employees have been laid off and that four (4) have also resigned. Without the Programme and the related charge, other employees are expected to leave and the restructuring may be put in jeopardy. According to MEI, the remaining employees are in a position of uncertainty in light of the many lay-offs. They need to be reassured.

12 MEI further indicates that it has the support of the National Bank of Canada for the creation of this charge. It adds that no objections have been raised by any of the creditors, even though it is not clear as to which ones were notified specifically of this pending request.

13 Neither MEI's counsel, nor the Court, found any precedent in the Quebec or Canadian case law on this issue. Apparently, no decision rendered in the context of a *CCAA* restructuring has specifically authorized the creation of a charge similar to the Employee Retention Charge sought here. Short of pure speculation, it is not possible to explain this absence of precedent. It is however sufficient for the Court to act with caution before granting MEI's request.

14 Notwithstanding its designation, MEI's counsel first submits that in reality, this charge is exactly the same as, and is finally no different than, a Debtor in Possession (DIP) financing and its related priority charge.

15 For the purposes of this Judgment, the Court accepts this proposition. The Employee Retention Charge is

indeed comparable to a DIP financing to allow the debtor corporation to continue operating. The justification behind it is in fact similar.

16 MEI's counsel then pleads that this is a situation where the Court should give a large and liberal interpretation to the *CCAA* and exercise its inherent jurisdiction to grant the priority charge requested.

17 With all due respect, the Court disagrees with this other submission in the context of MEI's restructuring. Obviously, some explanations are necessary in support of this finding. They are as follows.

18 It is now settled in canadian jurisprudence that the *CCAA* is a remedial legislation which is to be given a large interpretation to facilitate its objectives[FN3]. The courts recognize that *CCAA*'s effectiveness in achieving its objectives is indeed dependent on a broad and flexible exercise of jurisdiction so as to facilitate a restructuring and continue the debtor as a going concern in the interim[FN4].

19 The Quebec courts share the same vision as to the liberal interpretation of the *CCAA* and as to the necessity to achieve its objectives[FN5].

20 In giving to the *CCAA* such large and liberal interpretation and in facilitating the achievement of its objectives, courts in this country have relied on their inherent jurisdiction, or alternatively on the broad jurisdiction under Section 11, as the source of judicial power to "fill in the gaps" or "put flesh on the bones" of the Act[FN6].

21 In a noteworthy opinion issued recently in the context of a *CCAA* restructuring, Blair J. of the Ontario Court of Appeal summarized what is to be understood by this concept of inherent jurisdiction:

> [34] Inherent jurisdiction is a power derived "from the very nature of the court as a superior court of law", permitting the court "to maintain its authority and to prevent its process being obstructed and abused". It embodies the authority of the judiciary to control its own process and the lawyers and other officials connected with the court and its process, in order "to uphold, to protect and to fulfill the judicial function of administering justice according to law in a regular, orderly and effective manner". See I.H. Jacob, "The Inherent Jurisdiction of the Court" (1970) 23 Current Legal Problems 27-28. In Halsbury's Laws of England, 4th ed. (London: Lexis-Nexis UK, 1973 -) vol. 37, at para. 14, the concept is described as follows:
>
> In sum, it may be said that the inherent jurisdiction of the court is a virile and viable doctrine, and has been defined as being the reserve or fund of powers, a residual source of powers, which the court may draw upon as necessary whenever it is just or equitable to do so, in particularly to ensure the observation of the due process of law, to prevent improper vexation or oppression, to do justice between the parties and to secure a fair trial between them.

22 Under the *CCAA*, a well-known demonstration of the use of this inherent jurisdiction as a source of judicial power has been the courts' interpretation that it includes the ability to order DIP financing or create priority charges. As a matter of fact, one can safely venture to say that canadian courts have regularly affirmed their ability to create and order priority charges or priming liens in *CCAA* proceedings, be it to allow DIP financing or to cover D&O charges or administration charges[FN7].

23 Professor Janis Sarra, a well-respected author on the subject, provides a very good summary of the canadian courts' jurisdiction to grant such DIP financing and other priority charges or priming liens:

> The courts have interpreted their jurisdiction as including the ability to order DIP financing to allow corporations to continue operating during the stay period under the *CCAA*. Similarly, the courts have consistently affirmed their ability to order priming liens or priority charges in favour of insolvency officers during a *CCAA* proceeding. This allows the debtor corporation access to the professional services of the monitor, chief restructuring officer, other workout experts and lawyers that can assist with a successful workout. Such financing orders have been approved by the courts to cover administrative charges in a *CCAA* proceeding; to protect directors and officers from liability exposure; for specific environmental maintenance programs; to cover expenses and fees of a representative creditor and its legal counsel; insurance premium payments for director liability policies or for property and casualty coverage; and for general operating purposes, including post-petition trade creditor charges. DIP financing was approved in *Consumers' Packaging Inc.*, including cross-border approval with the initial *CCAA* order recognized by the U.S. Court pursuant to s. 304 of Chapter 11 of the U.S. *Bankruptcy Code*. The court has allowed the charge to cover the cost of insolvency professionals in preparation for the filing, but not work prior to contemplation of *CCAA* proceedings.
>
> The courts have found authority for granting super-priority charges or DIP financing under both the *CCAA* and their inherent jurisdiction. (. . .)[FN8]
>
> (Footnotes omitted)

24 While according to some[FN9], the question is still open as to whether or not the Quebec Superior Court can create such priority charges in Civil Law under the authority of its inherent jurisdiction, the case law in this Province[FN10] indicates that it has been done often in the context of *CCAA* proceedings, similarly to what has been seen in the rest of Canada.

25 That said, the review of the jurisprudence and doctrine on this issue of the exercise of the Courts' inherent jurisdiction to allow a DIP financing or create priority charges point out to the following factors, while not necessarily exhaustive, as applicable guidelines:

> 1) Allowing a DIP financing or creating a priority charge is an extraordinary measure that should be used sparingly and only in clear cases;
>
> 2) Before allowing a DIP financing or creating a priority charge, a court should be satisfied with proper evidence that the benefits to all creditors, shareholders and employees clearly outweigh the potential prejudice to some creditors;
>
> 3) It is not sufficient for the debtor to establish that the charge would be merely beneficial. It must rather establish that it is critical for the business to continue operating and to successfully restructure its affairs;
>
> 4) The debtor should normally establish an urgent need for the creation of the charge;

5) For a court to decide to create such a priority charge, there must be a reasonable prospect of a successful restructuring;

6) As it is an extraordinary remedy, the charge should only be available in limited amounts, for a brief period during the workout process, for what is enough to allow the debtor to "keep the lights on";

7) As the creation of such priority charge involves the use of its inherent jurisdiction powers, before drawing upon it, a court should be satisfied that it is just and equitable to do so in the given circumstances.

26 Bearing these in mind, the Court is of the view that many reasons explain why this case is not one where it should exercise its inherent jurisdiction to allow the creation of the Employee Retention Charge sought:

a) The Employee Retention Charge is aimed at guaranteeing the payment of the base amounts of the Programme to the employees covered, regardless of the outcome of the CCAA proceedings. Hence, the guarantee exists even if the CCAA process fails and ends up in a liquidation.

It is rather difficult to justify the creation of a priority charge in this context when the case law suggests that courts should make orders for priority charges only when there exists a reasonable prospect of a successful restructuring[FN11].

b) The Employee Retention Charge would, in essence, entail the financing of a "salary increase" for MEI's remaining employees by its unsecured creditors. These include trade creditors and employees, many of whom not only have no such salary increase but also lost their employment.

Thus, as a result, these "salary increase" claims of the employees remaining on board will be better protected than the claims of those who are now unemployed. It is difficult to see how this can be qualified as just and equitable.

c) In the same vein, creating a charge to guarantee the payment of the base amounts of the Employee Retention Programme (which are again, in reality, a "salary increase" for the employees staying on board during the restructuring process) is hard to justify when the other unsecured creditors (including trade suppliers and employees) will, in all likelihood, be paid far less than 100 % of their outstanding claims.

The balance that must exist between interest and prejudice amongst creditors of a same class does not appear to be present here.

d) Notwithstanding MEI's representations to the effect that the charge is necessary to allow the company to complete its restructuring for the benefit of all creditors, the burden of the charge is not shared equitably between MEI's creditors.

If this Employee Retention Charge is indeed key for MEI to successfully restructure itself under the *CCAA*, it is then difficult to understand why the charge is created only at the expense of the unsecured creditors, and not the secured ones. According to the testimony of the Monitor, the secured creditors will benefit directly from a successful restructuring, since a failure of the *CCAA* process may lead to a situation where even they will not be paid in full.

Yet, the ranking of the Employee Retention Charge after all the existing security on the assets of MEI entails that they are not sharing its cost in any manner, as opposed to the unsecured creditors who end up supporting its whole burden alone.

e) According to the cash flow projections filed[FN12], the average outstanding balance in MEI's bank account for all the weeks ending from April 30th, 2005 to July 2nd, 2005 is $531,873. Contrary to what was noted by the British Columbia Court of Appeal in another case, MEI's situation is not one where the cash flow from operations is insufficient to assure payment and where granting a super-priority is the only practical mean of securing the payment sought[FN13].

Considering these cash flow projections, there appears to be other practical ways to structure the payment of the base amounts of the Employee Retention Programme and to reassure the employees so that they stay on board.

For instance, these base amounts could be paid in "tranches" to the employees over a period of two or three months, with a similar commitment of MEI towards the full payment of the amounts contemplated by the end of the *CCAA* proceedings. The cash flow projections seem to allow for it and paying the amounts progressively would likely alleviate any negative impact.

In all likelihood, the employees could be as much reassured by a commitment of the company where they are being paid their money faster than by a commitment guaranteed by a priority charge where they will only see the colour of their money at the very end of the whole process, with the potential difficulties that a negative outcome may bring about for them.

f) Finally, under all the circumstances detailed above, the Court is not convinced by the evidence that this is a situation where it is urgent that this Employee Retention Charge be created to allow MEI to ""keep the lights on". In short, this is not a clear case where the exercise of the Court's judgment warrants the creation of this additional charge.

To that end, an analogy, albeit imperfect, can be drawn between the present situation and the one that existed in two decisions where, in the context of *CCAA* proceedings, the courts refused the creation of a charge to secure the payment of severance or termination pay to some employees as opposed to others. [FN14]

27 In closing, even though MEI's counsel strenuously argued that in the case at bar, there was no opposition raised and, as a result, the creation of the Employee Retention Charge would not stand as a precedent for other similar *CCAA* proceedings, the Court considers that this is certainly insufficient to grant the request sought. The lack of opposition is not a good enough reason for the Court to be lenient in a situation where the criteria recognized by the jurisprudence for the granting of priority charges are not otherwise met.

28 **FOR THESE REASONS, THE COURT:**

[2005] R.J.Q. 1558, EYB 2005-90239, J.E. 2005-1009, 19 C.B.R. (5th) 257

29 **DISMISSES** MEI's request for the creation of an Employee Retention Charge;

30 **WITHOUT COSTS.**

Application dismissed.

FN1. *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36.

FN2. Exhibit P-4.

FN3. *Stelco Inc., Re*, [2005] O.J. No. 1171 (Ont. C.A.) [*Stelco*], at ¶ 32.

FN4. *United Used Auto & Truck Parts Ltd., Re*, [2000] B.C.J. No. 409 (B.C. C.A.), at ¶ 12.

FN5. *PCI Chemicals Canada Inc., Re*, [2002] R.J.Q. 1093 (Que. S.C.), at ¶ 58; cited with approval in *Mine Jeffrey inc., Re*, [2003] R.J.Q. 420 (Que. C.A.), at ¶ 32.

FN6. *Stelco, supra*, note 3.

FN7. See, for example, *United Used Auto & Truck Parts Ltd., Re, supra*, note 4; *Air Canada, Re*, [2003] O.J. No. 1157 (Ont. S.C.J. [Commercial List]); *Sulphur Corp. of Canada Ltd., Re* (2002), 35 C.B.R. (4th) 304 (Alta. Q.B.); *Hunters Trailer & Marine Ltd., Re* (2001), 27 C.B.R. (4th) 236 (Alta. Q.B.); *Royal Oak Mines Inc., Re* (1999), 7 C.B.R. (4th) 293 (Ont. Gen. Div. [Commercial List]); *Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106 (Ont. Gen. Div. [Commercial List]); and *Westar Mining Ltd., Re*, [1992] B.C.J. No. 1816 (B.C. S.C.).

FN8. Janis SARRA, "Exploring the Boundaries, Jurisdiction under the Companies' Creditors Arrangement Act", Vancouver, May 2004, at p. 18 and 19. See also Pamela L.J. HUFF and Linc A. ROGERS, "Fortune Favours the Bold: Lending in a CCAA Proceeding and Priority Charges to Facilitate Restructurings", (2004) 16 *Comm. Insol.* R. 57, and Janis SARRA, "Debtor in Possession Financing: The Jurisdiction of Canadian Courts to Grant Superpriority Financing in CCAA Applications", (2000) 23 *Dalhousie L.J.* 337.

FN9. See in this respect the article of Me Antoine LEDUC, "Les limites de la "juridiction inhérente" du Tribunal et le cas du financement débiteur-exploitant ("DIP Financing") en droit québécois", in the *Insight Annual Conference on Insolvabilité et restructuration commerciale*, Montreal, April 18 and 19, 2005.

FN10. The Initial or Extension Orders issued in the restructuring of Jetsgo Corporation, Papiers Gaspesia Inc., Mines Jeffrey Inc., Les Boutiques San Francisco Inc., Concert Industries Inc. and Microcell Communications Inc. are some examples of this trend.

FN11. *United Used Auto & Truck Parts Ltd., Re, supra*, note 4, at ¶ 30.

FN12. Exhibit P-2.

FN13. *United Used Auto & Truck Parts Ltd., Re, supra*, note 4, at ¶ 29.

FN14. *Westar Mining Ltd., Re*, [1992] B.C.J. No. 1816 (B.C. S.C.); *Pacific National Lease Holding Corp., Re*, [1992] B.C.J. No. 3070 (B.C. S.C.).

END OF DOCUMENT

TAB 3

2009 CarswellOnt 1330

Nortel Networks Corp., Re
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 Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Global Corporation, Nortel Networks International Corporation and Nortel Networks Technology Corporation (the "Applicants")
Application under the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended
Ontario Superior Court of Justice [Commercial List]
Morawetz J.
Heard: March 6, 2009
Judgment: March 12, 2009
Docket: 09-CL-7950, 09-CL-7951

Counsel: Derrick Tay, Jennifer Stam for Nortel Networks Corporation, et al

J. Pasquariello for Monitor, Ernst & Young Inc.

Jonathan Bell for Informal Group of Nortel Networks Noteholders

R. Moncur, M. Barrack for Flextronics

M. Starnino for Pension Benefits Guarantee Fund

Harvey Chaiton for IBM

D. Ullman for Verizon Communications Inc.

Harvey Garman for U.K. Protection Fund, Nortel Networks UK Pension Trust Limited

Demtrios iokaris for Certain Former Salaried Employees of Nortel Networks

Alex MacFarlane for U.S. Unsecured Creditors' Committee

Subject: Insolvency; Corporate and Commercial

Bankruptcy and insolvency --- Proposal -- Companies' Creditors Arrangement Act -- Arrangements -- Approval by court -- "Fair and reasonable".

Cases considered by Morawetz J.:

Sierra Club of Canada v. Canada (Minister of Finance) (2002), 287 N.R. 203, (sub nom. Atomic Energy of Canada Ltd. v. Sierra Club of Canada) 18 C.P.R. (4th) 1, 44 C.E.L.R. (N.S.) 161, (sub nom. Atomic Energy of Canada Ltd. v. Sierra Club of Canada) 211 D.L.R. (4th) 193, 223 F.T.R. 137 (note), 20 C.P.C. (5th) 1, 40 Admin. L.R. (3d) 1, 2002 SCC 41, 2002 CarswellNat 822, 2002 CarswellNat 823, (sub nom. Atomic Energy of Canada Ltd. v. Sierra Club of Canada) 93 C.R.R. (2d) 219, [2002] 2 S.C.R. 522 (S.C.C.) -- followed

Statutes considered:

Bankruptcy Code, 11 U.S.C.

Generally -- referred to

Morawetz J.:

1 This motion was heard on March 6, 2009 and the requested relief was granted, with brief reasons to follow.

2 At the outset of the Nortel proceedings on January 14, 2009, Mr. Tay, on behalf of Nortel Networks Corporation (the "Applicants or Nortel"), indicated that the Applicants would be seeking approval of a Key Employee Incentive Plan ("KEIP") and a Key Employee Retention Plan ("KERP"). Such approval was sought on this motion, together with a request to approve the Calgary Retention Plan (the "Calgary Retention Plan") providing for retention bonus payments promised to employees in connection with the closing of the Westwinds facility.

3 This motion was not opposed.

4 The record establishes that the commitment and retention of key employees will be essential to the execution of a restructuring of Nortel and the completion of a plan of arrangement.

5 The KEIP applies to certain executives of the Senior Leadership Team ("SLTs") and the Executive Leadership Team ("ELTs") and the KERP applies to certain other key employees.

6 The Monitor reports that these plans have been developed to incent those employees who are:

(i) absolutely key to the success of the restructuring; and

(ii) to remain with the Applicants and U.S. Debtors through to the completion of the Canadian and U.S. proceedings

7 In designing the plans, Nortel obtained independent advice from Mercer (U.S.) Inc. ("Mercer") which included benchmarking total direct compensation levels against industry standards in comparing other key employee incentive plans approved by the courts in recent comparable North American restructurings. In addition, the Monitor reports that Nortel's financial advisor, Lezard Fréres & Co., as well as the Monitor were consulted by Nortel throughout the development process with respect to the plans and have provided Nortel with appropriate input.

8 A total of 972 employees are eligible for the plans. This represents approximately 5% of Nortel's global workforce (excluding employees of the EMEA Filed Entities and the joint venturers). The KEIP covers 92 participants, of which, 29 are employed by the Applicants. The potential dollar value to be paid out under the KEIP is approximately $23 million, of which $6.8 million is allocated to the Canadian Applicants. With respect to the KERP, this plan covers 880 participants, of which 294 are employed by the Canadian Applicants. The total potential dollar value to be paid out under the KERP is approximately $22 million, of which $6.2 million is allocated to the Canadian Applicants.

9 The awards under both the KEIP and the KERP will vest based on the achievement of three milestones, namely, achievement of North American objectives; achievement of certain parameters that will result in a leaner and more focussed organization; and court-approved confirmation of a plan of restructuring.

10 The Unsecured Creditors' Committee ("UCC") in the Chapter 11 proceedings has indicated that it supports the plans, although such support with respect to the KEIP for the SLTs is conditional upon the delivery to the UCC of Nortel's 2009 financial projections.

11 Counsel to the Applicants advised that the U.S. Bankruptcy Court has approved the KEIP (except as it relates to the SLTs) and the KERP.

12 In order to maintain consistency between Canada and the U.S., the Applicants' motion to approve the KEIP excludes the SLTs. The Monitor reports that the Applicants have advised that they intend to request approval of the KEIP for the SLTs at a future date.

13 With respect to the Calgary Retention Plan, a decision was made in July 2008 to close the Westwinds facility and transfer R & D and global operations to other facilities over a period of 12 months. In July 2008, Nortel developed the Calgary Retention Plan that provided for retention payments to be made to those Westwinds facility employees who Nortel determined were critical to the successful shutdown of the facility. The Applicants have indicated that the maximum cost of the Calgary Retention Plan is estimated to be approximately $727,000 to be paid to 45 employees at the time the employees have completed their portion of the project.

14 I am satisfied that the record establishes that the employees who are covered by the KEIP, the KERP and the Calgary Retention Plan are key to the operations of Nortel and are sought after by competitors, even given current market conditions.

15 The Monitor has reviewed the details of the Applicants proposed plans and Mercer's analysis and believes that the proposed plans provide reasonable compensation in the current situation.

16 Full details with respect to the plans are contained in the Confidential Report. I have reviewed this Report and agree with the submissions of both the Applicants and the Monitor that the Report contains sensitive commercial information that would be harmful to the Applicants if it were disclosed in the marketplace. In addition, the Confidential Report contains sensitive personal information relating to Nortel's employees, the disclosure of which, in my view, would be harmful.

17 The Applicants and the Monitor request that the Confidential Report be sealed, pending further order of the court. I am satisfied that the test for sealing the Confidential Report, as set out in *Sierra Club of Canada v.*

Canada (Minister of Finance), [2002] 2 S.C.R. 522 (S.C.C.)has been satisfied and it is appropriate to grant the sealing order.

18 I have been satisfied that it is appropriate to approve the plans in question.

19 An order shall therefore issue approving:

(i) the KEIP except as it relates to the Applicants' employees whose are designated members of the SLT;

(ii) the KERP; and

(iii) the Calgary Retention Plan

20 An order shall issue sealing the Confidential Report pending further order of this court.

END OF DOCUMENT

2009 CarswellOnt 1519

Nortel Networks Corp., Re
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 NORTEL NETWORKS CORPORATION, NORTEL NETWORKS LIMITED, NORTEL NETWORKS GLOBAL CORPORATION, NORTEL NETWORKS INTERNATIONAL CORPORATION AND NORTEL NETWORKS TECHNOLOGY CORPORATION (Applicants)
Ontario Superior Court of Justice [Commercial List]
Morawetz J.
Heard: March 20, 2009
Judgment: March 20, 2009
Docket: 09-CL-7950

Counsel: Derrick Tay, Jennifer Stam for Nortel Networks Corporation, et al

Mark Zigler, Demetrios Yiokaris for Former Employees of Nortel Networks

Eliezer Karp for Committee for the Nortel Canadian Terminated Employees Owed Termination and Severance Pay

Kevin Zych for Informal Nortel Noteholder Group

Lyndon Barnes for Boards of Directors of Nortel Networks Corporation and Nortel Networks Limited

Rachelle Moncur for Flextronics Telecom Systems Ltd.

Harvey Garman for UK Pension Protection Fund, Nortel Networks UK Pension Trust Limited

Max Starnino for Superintendent of Financial Services as Administrator of the Pension Benefits Guarantee Fund

Alex MacFarlane for Official Committee of Unsecured Creditors

J. Pasquariello for Monitor, Ernst & Young Inc.

Edmond Lamek for Export Development Canada

Subject: Insolvency

Bankruptcy and insolvency --- Proposal -- Companies' Creditors Arrangement Act -- Arrangements -- Approval by court -- "Fair and reasonable".

Cases considered by Morawetz J.:

Nortel Networks Corp., Re (2009), 2009 CarswellOnt 1330 (Ont. S.C.J. [Commercial List]) -- referred to

Statutes considered:

Bankruptcy Code, 11 U.S.C.

Chapter 11 -- referred to

Morawetz J.:

1 The Applicants move for approval of the key executive incentive plan ("KEIP") as it relates to the Applicants' senior leadership team ("SLT").

2 Counsel to the Applicants pointed out that the issues surrounding the KEIP have already been the subject of a previous motion. Mr. Tay made extensive references to my endorsement released March 12, 2009 [2009 CarswellOnt 1330 (Ont. S.C.J. [Commercial List])], which provided the reasons for the granting of the order of March 6, 2009, which order approved the KEIP, except as it related to the SLTs and which order also approved the key employee retention plan ("KERP").

3 The issue for today is whether it is appropriate to approve the KEIP as it relates to the SLTs.

4 Counsel advised that this issue is also being considered in the Chapter 11 proceedings today, and that the Chapter 11 application on this point is proceeding without opposition from the Unsecured Creditors' Committee.

5 Counsel also advised that the KEIP applies to 29 employees of the Applicants of which 8 are members of the SLT and that of the potential $23 million to be paid out under the KEIP, the amount allocated to the Canadian Applicants is $6.8 million.

6 Although the amounts involved are not insignificant, it is necessary, in my view, to consider the KEIP in the context of the overall restructuring. In this respect, the endorsement should be read in conjunction with my reasons relating to the KERP and KEIP approval motion, (reasons of March 12, 2009) in which certain findings were made that supported the relief granted at that time.

7 The submissions of Mr. Tay were supported by Mr. Barnes on behalf of the Board of Directors. Mr. Barnes added that the Board could not function without an experienced leadership team and that the potential loss of management at this time could be very detrimental. Mr. Barnes also reiterated the complexity of the Nortel restructuring.

8 The Monitor also expressed its support of the Applicants' motion.

9 Mr. Zigler, on behalf of 2000 former employees noted, with some reluctance, that his clients do not object to the relief sought, but in so doing he made it clear that both he and counsel to the Applicants have represented to the Court that none of the milestones which would result in payments under the KEIP program are tied to a

reduction of any pension funding payments or benefits currently being paid to or in respect of former employees or pensioners.

10 I note that the same representation was made to the Court during submissions at the March 6, 2009 hear- ing.

11 The only party who opposed the relief sought on the KEIP issue was Mr. Karp, on behalf of 60 severed employees. This group, according to Mr. Karp, could expand to 1,100 and his status is expected to be the subject of an upcoming motion in which he will be seeking Representative Counsel status. Mr. Karp objects to the proposed payments under the KEIP noting that his clients are not receiving severance payments.

12 Mr. Karp also advised that he has not taken any steps to appeal my decision of March 6, 2009.

13 Having considered the foregoing submissions, the approval sought today in respect of the KEIP is, in my view, consistent with prior approval of the KEIP and that the reasons applicable to the approval and implementation of both the KERP and the KEIP as they relate to the Applicants' employees (other than SLTs) are equally applicable to the Applicants' SLTs. An order shall issue granting the requested relief relating to the KEIP.

14 The Applicants also seek relief relating to the Termination of Change in Control Plan and the treatment of certain personal information of employees. The relief sought in both areas was not opposed and the record establishes that the requested relief is appropriate and it is granted.

15 An order shall issue in the form presented.

END OF DOCUMENT

TAB 4

7 C.B.R. (3d) 1, 4 O.R. (3d) 1, 83 D.L.R. (4th) 76, 46 O.A.C. 321

1991 CarswellOnt 205

Royal Bank v. Soundair Corp.
ROYAL BANK OF CANADA (plaintiff/respondent) v. SOUNDAIR CORPORATION (respondent), CANADIAN PENSION CAPITAL LIMITED (appellant) and CANADIAN INSURERS' CAPITAL CORPORATION (appellant)
Ontario Court of Appeal
Goodman, McKinlay and Galligan JJ.A.
Heard: June 11, 12, 13 and 14, 1991
Judgment: July 3, 1991
Docket: Doc. CA 318/91

Counsel: J. B. Berkow and S. H. Goldman, for appellants Canadian Pension Capital Limited and Canadian Insurers' Capital Corporation.

J. T. Morin, Q.C., for Air Canada.

L.A.J. Barnes and L.E. Ritchie, for plaintiff/respondent Royal Bank of Canada.

S.F. Dunphy and G.K. Ketcheson, for Ernst & Young Inc., receiver of respondent Soundair Corporation.

W.G. Horton, for Ontario Express Limited.

N.J. Spies, for Frontier Air Limited.

Subject: Corporate and Commercial; Insolvency

Receivers --- Conduct and liability of receiver -- General conduct of receiver.

Receivers -- Sale of debtor's assets -- Approval by court -- Court appointing receiver to sell airline as going concern -- Court considering its position when approving sale recommended by receiver.

S Corp., which engaged in the air transport business, had a division known as AT. When S Corp. experienced financial difficulties, one of the secured creditors, who had an interest in the assets of AT, brought a motion for the appointment of a receiver. The receiver was ordered to operate AT and to sell it as a going concern. The receiver had two offers. It accepted the offer made by OEL and rejected an offer by 922 which contained an unacceptable condition. Subsequently, 922 obtained an order allowing it to make a second offer removing the condition. The secured creditors supported acceptance of the 922 offer. The court approved the sale to OEL and dismissed the motion to approve the 922 offer. An appeal was brought from this order.

Held:

The appeal was dismissed.

Per Galligan J.A.: When a court appoints a receiver to use its commercial expertise to sell an airline, it is inescapable that it intends to rely upon the receiver's expertise and not upon its own. The court should be reluctant to second-guess, with the benefit of hindsight, the considered business decisions made by its receiver.

The conduct of the receiver should be reviewed in the light of the specific mandate given to him by the court. The order appointing the receiver did not say how the receiver was to negotiate the sale. The order obviously intended, because of the unusual nature of the asset being sold, to leave the method of sale substantially to the discretion of the receiver.

To determine whether a receiver has acted providently, the conduct of the receiver should be examined in light of the information the receiver had when it agreed to accept an offer. On the date the receiver accepted the OEL offer, it had only two offers: that of OEL, which was acceptable, and that of 922, which contained an unacceptable condition. The decision made was a sound one in the circumstances. The receiver made a sufficient effort to obtain the best price, and did not act improvidently.

The court must exercise extreme caution before it interferes with the process adopted by a receiver to sell an unusual asset. It is important that prospective purchasers know that, if they are acting in good faith, bargain seriously with a receiver and enter into an agreement with it, a court will not lightly interfere with the commercial judgment of the receiver to sell the assets to them.

Per McKinlay J.A. (concurring in the result): It is most important that the integrity of procedures followed by court-appointed receivers be protected in the interests of both commercial morality and the future confidence of business persons in their dealings with receivers. In all cases, the court should carefully scrutinize the procedure followed by the receiver. While the procedure carried out by the receiver in this case was appropriate, given the unfolding of events and the unique nature of the asset involved, it may not be a procedure that is likely to be appropriate in many receivership sales.

Per Goodman J.A. (dissenting): It was imprudent and unfair on the part of the receiver to ignore an offer from an interested party which offered approximately triple the cash down payment without giving a chance to the offeror to remove the conditions or other terms which made the offer unacceptable to the receiver. The offer accepted by the receiver was improvident and unfair insofar as two creditors were concerned.

Cases considered:

Beauty Counsellors of Canada Ltd., Re (1986), 58 C.B.R. (N.S.) 237 (Ont. S.C.) -- referred to

British Columbia Development Corp. v. Spun Cast Industries Ltd. (1977), 26 C.B.R. (N.S.) 28, 5 B.C.L.R. 94 (S.C.) -- referred to

Cameron v. Bank of Nova Scotia (1981), 38 C.B.R. (N.S.) 1, 45 N.S.R. (2d) 303, 86 A.P.R. 303 (C.A.) -- referred to

Crown Trust Co. v. Rosenburg (1986), 67 C.B.R. (N.S.) 320n, 60 O.R. (2d) 87, 22 C.P.C. (2d) 131, 39 D.L.R. (4th) 526 (H.C.) -- applied

Salima Investments Ltd. v. Bank of Montreal (1985), 59 C.B.R. (N.S.) 242, 41 Alta. L.R. (2d) 58, 65 A.R. 372, 21 D.L.R. (4th) (C.A.) -- referred to

Selkirk, Re (1986), 58 C.B.R. (N.S.) 245 (Ont. S.C.) -- referred to

Selkirk, Re (1987), 64 C.B.R. (N.S.) 140 (Ont. S.C.) -- referred to

Statutes considered:

Employment Standards Act, R.S.O. 1980, c. 137.

Environmental Protection Act, R.S.O. 1980, c. 141.

Appeal from order approving sale of assets by receiver.

***Galligan J.A.*:**

1 This is an appeal from the order of Rosenberg J. made on May 1, 1991. By that order, he approved the sale of Air Toronto to Ontario Express Limited and Frontier Air Limited, and he dismissed a motion to approve an offer to purchase Air Toronto by 922246 Ontario Limited.

2 It is necessary at the outset to give some background to the dispute. Soundair Corporation ("Soundair") is a corporation engaged in the air transport business. It has three divisions. One of them is Air Toronto. Air Toronto operates a scheduled airline from Toronto to a number of mid-sized cities in the United States of America. Its routes serve as feeders to several of Air Canada's routes. Pursuant to a connector agreement, Air Canada provides some services to Air Toronto and benefits from the feeder traffic provided by it. The operational relationship between Air Canada and Air Toronto is a close one.

3 In the latter part of 1989 and the early part of 1990, Soundair was in financial difficulty. Soundair has two secured creditors who have an interest in the assets of Air Toronto. The Royal Bank of Canada (the "Royal Bank") is owed at least $65 million dollars. The appellants Canadian Pension Capital Limited and Canadian Insurers' Capital Corporation (collectively called "CCFL") are owed approximately $9,500,000. Those creditors will have a deficiency expected to be in excess of $50 million on the winding up of Soundair.

4 On April 26, 1990, upon the motion of the Royal Bank, O'Brien J. appointed Ernst & Young Inc. (the "receiver") as receiver of all of the assets, property and undertakings of Soundair. The order required the receiver to operate Air Toronto and sell it as a going concern. Because of the close relationship between Air Toronto and Air Canada, it was contemplated that the receiver would obtain the assistance of Air Canada to operate Air Toronto. The order authorized the receiver:

> (b) to enter into contractual arrangements with Air Canada to retain a manager or operator, including Air Canada, to manage and operate Air Toronto under the supervision of Ernst & Young Inc. until the completion of the sale of Air Toronto to Air Canada or other person.

Also because of the close relationship, it was expected that Air Canada would purchase Air Toronto. To that end, the order of O'Brien J. authorized the Receiver:

(c) to negotiate and do all things necessary or desirable to complete a sale of Air Toronto to Air Canada and, if a sale to Air Canada cannot be completed, to negotiate and sell Air Toronto to another person, subject to terms and conditions approved by this Court.

5 Over a period of several weeks following that order, negotiations directed towards the sale of Air Toronto took place between the receiver and Air Canada. Air Canada had an agreement with the receiver that it would have exclusive negotiating rights during that period. I do not think it is necessary to review those negotiations, but I note that Air Canada had complete access to all of the operations of Air Toronto and conducted due diligence examinations. It became thoroughly acquainted with every aspect of Air Toronto's operations.

6 Those negotiations came to an end when an offer made by Air Canada on June 19, 1990, was considered unsatisfactory by the receiver. The offer was not accepted and lapsed. Having regard to the tenor of Air Canada's negotiating stance and a letter sent by its solicitors on July 20, 1990, I think that the receiver was eminently reasonable when it decided that there was no realistic possibility of selling Air Toronto to Air Canada.

7 The receiver then looked elsewhere. Air Toronto's feeder business is very attractive, but it only has value to a national airline. The receiver concluded reasonably, therefore, that it was commercially necessary for one of Canada's two national airlines to be involved in any sale of Air Toronto. Realistically, there were only two possible purchasers, whether direct or indirect. They were Air Canada and Canadian Airlines International.

8 It was well known in the air transport industry that Air Toronto was for sale. During the months following the collapse of the negotiations with Air Canada, the receiver tried unsuccessfully to find viable purchasers. In late 1990, the receiver turned to Canadian Airlines International, the only realistic alternative. Negotiations began between them. Those negotiations led to a letter of intent dated February 11, 1990. On March 6, 1991, the receiver received an offer from Ontario Express Limited and Frontier Airlines Limited, who are subsidiaries of Canadian Airlines International. This offer is called the OEL offer.

9 In the meantime, Air Canada and CCFL were having discussions about making an offer for the purchase of Air Toronto. They formed 922246 Ontario Limited ("922") for the purpose of purchasing Air Toronto. On March 1, 1991, CCFL wrote to the receiver saying that it proposed to make an offer. On March 7, 1991, Air Canada and CCFL presented an offer to the receiver in the name of 922. For convenience, its offers are called the "922 offers."

10 The first 922 offer contained a condition which was unacceptable to the receiver. I will refer to that condition in more detail later. The receiver declined the 922 offer and on March 8, 1991, accepted the OEL offer. Subsequently, 922 obtained an order allowing it to make a second offer. It then submitted an offer which was virtually identical to that of March 7, 1991, except that the unacceptable condition had been removed.

11 The proceedings before Rosenberg J. then followed. He approved the sale to OEL and dismissed a motion for the acceptance of the 922 offer. Before Rosenberg J., and in this court, both CCFL and the Royal Bank supported the acceptance of the second 922 offer.

12 There are only two issues which must be resolved in this appeal. They are:

(1) Did the receiver act properly when it entered into an agreement to sell Air Toronto to OEL?

(2) What effect does the support of the 922 offer by the secured creditors have on the result?

13 I will deal with the two issues separately.

1. Did the Receiver Act Properly in Agreeing to Sell to OEL?

14 Before dealing with that issue, there are three general observations which I think I should make. The first is that the sale of an airline as a going concern is a very complex process. The best method of selling an airline at the best price is something far removed from the expertise of a court. When a court appoints a receiver to use its commercial expertise to sell an airline, it is inescapable that it intends to rely upon the receiver's expertise and not upon its own. Therefore, the court must place a great deal of confidence in the actions taken and in the opinions formed by the receiver. It should also assume that the receiver is acting properly unless the contrary is clearly shown. The second observation is that the court should be reluctant to second-guess, with the benefit of hindsight, the considered business decisions made by its receiver. The third observation which I wish to make is that the conduct of the receiver should be reviewed in the light of the specific mandate given to him by the court.

15 The order of O'Brien J. provided that if the receiver could not complete the sale to Air Canada that it was "to negotiate and sell Air Toronto to another person." The court did not say how the receiver was to negotiate the sale. It did not say it was to call for bids or conduct an auction. It told the receiver to negotiate and sell. It obviously intended, because of the unusual nature of the asset being sold, to leave the method of sale substantially in the discretion of the receiver. I think, therefore, that the court should not review minutely the process of the sale when, broadly speaking, it appears to the court to be a just process.

16 As did Rosenberg J., I adopt as correct the statement made by Anderson J. in *Crown Trust Co. v. Rosenberg* (1986), 60 O.R. (2d) 87, 67 C.B.R. (N.S.) 320n, 22 C.P.C. (2d) 131, 39 D.L.R. (4th) 526 (H.C.), at pp. 92-94 [O.R.], of the duties which a court must perform when deciding whether a receiver who has sold a property acted properly. When he set out the court's duties, he did not put them in any order of priority, nor do I. I summarize those duties as follows:

1. It should consider whether the receiver has made a sufficient effort to get the best price and has not acted improvidently.

2. It should consider the interests of all parties.

3. It should consider the efficacy and integrity of the process by which offers are obtained.

4. It should consider whether there has been unfairness in the working out of the process.

17 I intend to discuss the performance of those duties separately.

1. Did the Receiver make a sufficient effort to get the best price and did it act providently?

18 Having regard to the fact that it was highly unlikely that a commercially viable sale could be made to anyone but the two national airlines, or to someone supported by either of them, it is my view that the receiver acted wisely and reasonably when it negotiated only with Air Canada and Canadian Airlines International. Furthermore, when Air Canada said that it would submit no further offers and gave the impression that it would not par-

ticipate further in the receiver's efforts to sell, the only course reasonably open to the receiver was to negotiate with Canadian Airlines International. Realistically, there was nowhere else to go but to Canadian Airlines International. In doing so, it is my opinion that the receiver made sufficient efforts to sell the airline.

19 When the receiver got the OEL offer on March 6, 1991, it was over 10 months since it had been charged with the responsibility of selling Air Toronto. Until then, the receiver had not received one offer which it thought was acceptable. After substantial efforts to sell the airline over that period, I find it difficult to think that the receiver acted improvidently in accepting the only acceptable offer which it had.

20 On March 8, 1991, the date when the receiver accepted the OEL offer, it had only two offers, the OEL offer, which was acceptable, and the 922 offer, which contained an unacceptable condition. I cannot see how the receiver, assuming for the moment that the price was reasonable, could have done anything but accept the OEL offer.

21 When deciding whether a receiver had acted providently, the court should examine the conduct of the receiver in light of the information the receiver had when it agreed to accept an offer. In this case, the court should look at the receiver's conduct in the light of the information it had when it made its decision on March 8, 1991. The court should be very cautious before deciding that the receiver's conduct was improvident based upon information which has come to light after it made its decision. To do so, in my view, would derogate from the mandate to sell given to the receiver by the order of O'Brien J. I agree with and adopt what was said by Anderson J. in *Crown Trust Co. v. Rosenberg*, supra, at p. 112 [O.R.]:

> Its decision was made as a matter of business judgment *on the elements then available to it.* It is of the very essence of a receiver's function to make such judgments and in the making of them to act seriously and responsibly so as to be prepared to stand behind them.
>
> If the court were to reject the recommendation of the Receiver in any but the most exceptional circumstances, it would materially diminish and weaken the role and function of the Receiver both in the perception of receivers and in the perception of any others who might have occasion to deal with them. It would lead to the conclusion that the decision of the Receiver was of little weight and that the real decision was always made upon the motion for approval. That would be a consequence susceptible of immensely damaging results to the disposition of assets by court-appointed receivers.

[Emphasis added.]

22 I also agree with and adopt what was said by Macdonald J.A. in *Cameron v. Bank of Nova Scotia* (1981), 38 C.B.R. (N.S.) 1, 45 N.S.R. (2d) 303, 86 A.P.R. 303 (C.A.), at p. 11 [C.B.R.]:

> In my opinion if the decision of the receiver to enter into an agreement of sale, subject to court approval, with respect to certain assets is reasonable and sound under the circumstances *at the time existing* it should not be set aside simply because a later and higher bid is made. To do so would literally create chaos in the commercial world and receivers and purchasers would never be sure they had a binding agreement.

[Emphasis added.]

23 On March 8, 1991, the receiver had two offers. One was the OEL offer, which it considered satisfactory but which could be withdrawn by OEL at any time before it was accepted. The receiver also had the 922 offer, which contained a condition that was totally unacceptable. It had no other offers. It was faced with the dilemma of whether it should decline to accept the OEL offer and run the risk of it being withdrawn, in the hope that an acceptable offer would be forthcoming from 922. An affidavit filed by the president of the receiver describes the dilemma which the receiver faced, and the judgment made in the light of that dilemma:

> 24. An asset purchase agreement was received by Ernst & Young on March 7, 1991 which was dated March 6, 1991. This agreement was received from CCFL in respect of their offer to purchase the assets and undertaking of Air Toronto. Apart from financial considerations, which will be considered in a subsequent affidavit, the *Receiver determined that it would not be prudent to delay acceptance of the OEL agreement to negotiate a highly uncertain arrangement with Air Canada and CCFL.* Air Canada had the benefit of an 'exclusive' in negotiations for Air Toronto and had clearly indicated its intention take itself out of the running while ensuring that no other party could seek to purchase Air Toronto and maintain the Air Canada connector arrangement vital to its survival. The CCFL offer represented a radical reversal of this position by Air Canada at the eleventh hour. However, it contained a significant number of conditions to closing which were entirely beyond the control of the Receiver. As well, the CCFL offer came less than 24 hours before signing of the agreement with OEL which had been negotiated over a period of months, at great time and expense.

[Emphasis added.] I am convinced that the decision made was a sound one in the circumstances faced by the receiver on March 8, 1991.

24 I now turn to consider whether the price contained in the OEL offer was one which it was provident to accept. At the outset, I think that the fact that the OEL offer was the only acceptable one available to the receiver on March 8, 1991, after 10 months of trying to sell the airline, is strong evidence that the price in it was reasonable. In a deteriorating economy, I doubt that it would have been wise to wait any longer.

25 I mentioned earlier that, pursuant to an order, 922 was permitted to present a second offer. During the hearing of the appeal, counsel compared at great length the price contained in the second 922 offer with the price contained in the OEL offer. Counsel put forth various hypotheses supporting their contentions that one offer was better than the other.

26 It is my opinion that the price contained in the 922 offer is relevant only if it shows that the price obtained by the receiver in the OEL offer was not a reasonable one. In *Crown Trust Co. v. Rosenberg*, supra, Anderson J., at p. 113 [O.R.], discussed the comparison of offers in the following way:

> No doubt, as the cases have indicated, situations might arise where the disparity was so great as to call in question the adequacy of the mechanism which had produced the offers. It is not so here, and in my view that is substantially an end of the matter.

27 In two judgments, Saunders J. considered the circumstances in which an offer submitted after the receiver had agreed to a sale should be considered by the court. The first is *Re Selkirk* (1986), 58 C.B.R. (N.S.) 245 (Ont. S.C.), at p. 247:

> If, for example, in this case there had been a second offer of a substantially higher amount, then the court would have to take that offer into consideration in assessing whether the receiver had properly carried out his function of endeavouring to obtain the best price for the property.

28 The second is *Re Beauty Counsellors of Canada Ltd.* (1986), 58 C.B.R. (N.S.) 237 (Ont. S.C.), at p. 243:

> If a substantially higher bid turns up at the approval stage, the court should consider it. Such a bid may indicate, for example, that the trustee has not properly carried out its duty to endeavour to obtain the best price for the estate.

29 In *Re Selkirk* (1987), 64 C.B.R. (N.S.) 140 (Ont. S.C.), at p. 142, McRae J. expressed a similar view:

> The court will not lightly withhold approval of a sale by the receiver, particularly in a case such as this where the receiver is given rather wide discretionary authority as per the order of Mr. Justice Trainor and, of course, where the receiver is an officer of this court. Only in a case where there seems to be some unfairness in the process of the sale or *where there are substantially higher offers which would tend to show that the sale was improvident* will the court withhold approval. It is important that the court recognize the commercial exigencies that would flow if prospective purchasers are allowed to wait until the sale is in court for approval before submitting their final offer. This is something that must be discouraged.

[Emphasis added.]

30 What those cases show is that the prices in other offers have relevance only if they show that the price contained in the offer accepted by the receiver was so unreasonably low as to demonstrate that the receiver was improvident in accepting it. I am of the opinion, therefore, that if they do not tend to show that the receiver was improvident, they should not be considered upon a motion to confirm a sale recommended by a court-appointed receiver. If they were, the process would be changed from a sale by a receiver, subject to court approval, into an auction conducted by the court at the time approval is sought. In my opinion, the latter course is unfair to the person who has entered bona fide into an agreement with the receiver, can only lead to chaos, and must be discouraged.

31 If, however, the subsequent offer is so substantially higher than the sale recommended by the receiver, then it may be that the receiver has not conducted the sale properly. In such circumstances, the court would be justified itself in entering into the sale process by considering competitive bids. However, I think that that process should be entered into only if the court is satisfied that the receiver has not properly conducted the sale which it has recommended to the court.

32 It is necessary to consider the two offers. Rosenberg J. held that the 922 offer was slightly better or marginally better than the OEL offer. He concluded that the difference in the two offers did not show that the sale process adopted by the receiver was inadequate or improvident.

33 Counsel for the appellants complained about the manner in which Rosenberg J. conducted the hearing of the motion to confirm the OEL sale. The complaint was that when they began to discuss a comparison of the two offers, Rosenberg J. said that he considered the 922 offer to be better than the OEL offer. Counsel said that when

that comment was made, they did not think it necessary to argue further the question of the difference in value between the two offers. They complain that the finding that the 922 offer was only marginally better or slightly better than the OEL offer was made without them having had the opportunity to argue that the 922 offer was substantially better or significantly better than the OEL offer. I cannot understand how counsel could have thought that by expressing the opinion that the 922 offer was better, Rosenberg J. was saying that it was a significantly or substantially better one. Nor can I comprehend how counsel took the comment to mean that they were foreclosed from arguing that the offer was significantly or substantially better. If there was some misunderstanding on the part of counsel, it should have been raised before Rosenberg J. at the time. I am sure that if it had been, the misunderstanding would have been cleared up quickly. Nevertheless, this court permitted extensive argument dealing with the comparison of the two offers.

34 The 922 offer provided for $6 million cash to be paid on closing with a royalty based upon a percentage of Air Toronto profits over a period of 5 years up to a maximum of $3 million. The OEL offer provided for a payment of $2 million on closing with a royalty paid on gross revenues over a 5-year period. In the short term, the 922 offer is obviously better because there is substantially more cash up front. The chances of future returns are substantially greater in the OEL offer because royalties are paid on gross revenues, while the royalties under the 922 offer are paid only on profits. There is an element of risk involved in each offer.

35 The receiver studied the two offers. It compared them and took into account the risks, the advantages and the disadvantages of each. It considered the appropriate contingencies. It is not necessary to outline the factors which were taken into account by the receiver because the manager of its insolvency practice filed an affidavit outlining the considerations which were weighed in its evaluation of the two offers. They seem to me to be reasonable ones. That affidavit concluded with the following paragraph:

> 24. On the basis of these considerations the Receiver has approved the OEL offer and has concluded that it represents the achievement of the highest possible value at this time for the Air Toronto division of SoundAir.

36 The court appointed the receiver to conduct the sale of Air Toronto, and entrusted it with the responsibility of deciding what is the best offer. I put great weight upon the opinion of the receiver. It swore to the court which appointed it that the OEL offer represents the achievement of the highest possible value at this time for Air Toronto. I have not been convinced that the receiver was wrong when he made that assessment. I am, therefore, of the opinion that the 922 offer does not demonstrate any failure upon the part of the receiver to act properly and providently.

37 It follows that if Rosenberg J. was correct when he found that the 922 offer was in fact better, I agree with him that it could only have been slightly or marginally better. The 922 offer does not lead to an inference that the disposition strategy of the receiver was inadequate, unsuccessful or improvident, nor that the price was unreasonable.

38 I am, therefore, of the opinion the the receiver made a sufficient effort to get the best price, and has not acted improvidently.

2. Consideration of the Interests of all Parties

39 It is well established that the primary interest is that of the creditors of the debtor: see *Crown Trust Co. v. Rosenberg*, supra, and *Re Selkirk*, supra (Saunders J.). However, as Saunders J. pointed out in *Re Beauty Counsellors*, supra at p. 244 [C.B.R.], "it is not the only or overriding consideration."

40 In my opinion, there are other persons whose interests require consideration. In an appropriate case, the interests of the debtor must be taken into account. I think also, in a case such as this, where a purchaser has bargained at some length and doubtless at considerable expense with the receiver, the interests of the purchaser ought to be taken into account. While it is not explicitly stated in such cases as *Crown Trust Co. v. Rosenberg*, supra, *Re Selkirk* (1986), supra, *Re Beauty Counsellors*, supra, *Re Selkirk* (1987), supra, and (*Cameron*), supra, I think they clearly imply that the interests of a person who has negotiated an agreement with a court-appointed receiver are very important.

41 In this case, the interests of all parties who would have an interest in the process were considered by the receiver and by Rosenberg J.

3. Consideration of the Efficacy and Integrity of the Process by which the Offer was Obtained

42 While it is accepted that the primary concern of a receiver is the protecting of the interests of the creditors, there is a secondary but very important consideration, and that is the integrity of the process by which the sale is effected. This is particularly so in the case of a sale of such a unique asset as an airline as a going concern.

43 The importance of a court protecting the integrity of the process has been stated in a number of cases. First, I refer to *Re Selkirk*, supra, where Saunders J. said at p. 246 [C.B.R.]:

> In dealing with the request for approval, the court has to be concerned primarily with protecting the interest of the creditors of the former bankrupt. A secondary but important consideration is that the process under which the sale agreement is arrived at should be consistent with commercial efficacy and integrity.
>
> In that connection I adopt the principles stated by Macdonald J.A. of the Nova Scotia Supreme Court (Appeal Division) in *Cameron v. Bank of N.S.* (1981), 38 C.B.R. (N.S.) 1, 45 N.S.R. (2d) 303, 86 A.P.R. 303 (C.A.), where he said at p. 11:
>
>> In my opinion if the decision of the receiver to enter into an agreement of sale, subject to court approval, with respect to certain assets is reasonable and sound under the circumstances at the time existing it should not be set aside simply because a later and higher bid is made. To do so would literally create chaos in the commercial world and receivers and purchasers would never be sure they had a binding agreement. On the contrary, they would know that other bids could be received and considered up until the application for court approval is heard -- this would be an intolerable situ- ation.
>
> While those remarks may have been made in the context of a bidding situation rather than a private sale, I consider them to be equally applicable to a negotiation process leading to a private sale. Where the court is concerned with the disposition of property, the purpose of appointing a receiver is to have the receiver do the work that the court would otherwise have to do.

44 In *Salima Investments Ltd. v. Bank of Montreal* (1985), 59 C.B.R. (N.S.) 242, 41 Alta. L.R. (2d) 58, 65 A.R. 372, 21 D.L.R. (4th) 473 at p. 476 [D.L.R.], the Alberta Court of Appeal said that sale by tender is not necessarily the best way to sell a business as an ongoing concern. It went on to say that when some other method is used which is provident, the court should not undermine the process by refusing to confirm the sale.

45 Finally, I refer to the reasoning of Anderson J. in *Crown Trust Co. v. Rosenberg*, supra, at p. 124 [O.R.]:

> While every proper effort must always be made to assure maximum recovery consistent with the limitations inherent in the process, no method has yet been devised to entirely eliminate those limitations or to avoid their consequences. *Certainly it is not to be found in loosening the entire foundation of the system. Thus to compare the results of the process in this case with what might have been recovered in some other set of circumstances is neither logical nor practical.*

[Emphasis added.]

46 It is my opinion that the court must exercise extreme caution before it interferes with the process adopted by a receiver to sell an unusual asset. It is important that prospective purchasers know that, if they are acting in good faith, bargain seriously with a receiver and enter into an agreement with it, a court will not lightly interfere with the commercial judgment of the receiver to sell the asset to them.

47 Before this court, counsel for those opposing the confirmation of the sale to OEL suggested many different ways in which the receiver could have conducted the process other than the way which he did. However, the evidence does not convince me that the receiver used an improper method of attempting to sell the airline. The answer to those submissions is found in the comment of Anderson J. in *Crown Trust Co. v. Rosenberg*, supra, at p. 109 [O.R.]:

> The court ought not to sit as on appeal from the decision of the Receiver, reviewing in minute detail every element of the process by which the decision is reached. To do so would be a futile and duplicitous exercise.

48 It would be a futile and duplicitous exercise for this court to examine in minute detail all of circumstances leading up to the acceptance of the OEL offer. Having considered the process adopted by the receiver, it is my opinion that the process adopted was a reasonable and prudent one.

4. Was there unfairness in the process?

49 As a general rule, I do not think it appropriate for the court to go into the minutia of the process or of the selling strategy adopted by the receiver. However, the court has a responsibility to decide whether the process was fair. The only part of this process which I could find that might give even a superficial impression of unfairness is the failure of the receiver to give an offering memorandum to those who expressed an interest in the purchase of Air Toronto.

50 I will outline the circumstances which relate to the allegation that the receiver was unfair in failing to provide an offering memorandum. In the latter part of 1990, as part of its selling strategy, the receiver was in the process of preparing an offering memorandum to give to persons who expressed an interest in the purchase of

Air Toronto. The offering memorandum got as far as draft form, but was never released to anyone, although a copy of the draft eventually got into the hands of CCFL before it submitted the first 922 offer on March 7, 1991. A copy of the offering memorandum forms part of the record, and it seems to me to be little more than puffery, without any hard information which a sophisticated purchaser would require in order to make a serious bid.

51 The offering memorandum had not been completed by February11, 1991. On that date, the receiver entered into the letter of intent to negotiate with OEL. The letter of intent contained a provision that during its currency the receiver would not negotiate with any other party. The letter of intent was renewed from time to time until the OEL offer was received on March 6, 1991.

52 The receiver did not proceed with the offering memorandum because to do so would violate the spirit, if not the letter, of its letter of intent with OEL.

53 I do not think that the conduct of the receiver shows any unfairness towards 922. When I speak of 922, I do so in the context that Air Canada and CCFL are identified with it. I start by saying that the receiver acted reasonably when it entered into exclusive negotiations with OEL. I find it strange that a company, with which Air Canada is closely and intimately involved, would say that it was unfair for the receiver to enter into a time-limited agreement to negotiate exclusively with OEL. That is precisely the arrangement which Air Canada insisted upon when it negotiated with the receiver in the spring and summer of 1990. If it was not unfair for Air Canada to have such an agreement, I do not understand why it was unfair for OEL to have a similar one. In fact, both Air Canada and OEL in its turn were acting reasonably when they required exclusive negotiating rights to prevent their negotiations from being used as a bargaining lever with other potential purchasers. The fact that Air Canada insisted upon an exclusive negotiating right while it was negotiating with the receiver demonstrates the commercial efficacy of OEL being given the same right during its negotiations with the receiver. I see no unfairness on the part of the receiver when it honoured its letter of intent with OEL by not releasing the offering memorandum during the negotiations with OEL.

54 Moreover, I am not prepared to find that 922 was in any way prejudiced by the fact that it did not have an offering memorandum. It made an offer on March 7, 1991, which it contends to this day was a better offer than that of OEL. 922 has not convinced me that if it had an offering memorandum, its offer would have been any different or any better than it actually was. The fatal problem with the first 922 offer was that it contained a condition which was completely unacceptable to the receiver. The receiver, properly, in my opinion, rejected the offer out of hand because of that condition. That condition did not relate to any information which could have conceivably been in an offering memorandum prepared by the receiver. It was about the resolution of a dispute between CCFL and the Royal Bank, something the receiver knew nothing about.

55 Further evidence of the lack of prejudice which the absence of an offering memorandum has caused 922 is found in CCFL's stance before this court. During argument, its counsel suggested as a possible resolution of this appeal that this court should call for new bids, evaluate them and then order a sale to the party who put in the better bid. In such a case, counsel for CCFL said that 922 would be prepared to bid within 7 days of the court's decision. I would have thought that, if there were anything to CCFL's suggestion that the failure to provide an offering memorandum was unfair to 922, that it would have told the court that it needed more information before it would be able to make a bid.

56 I am satisfied that Air Canada and CCFL have, and at all times had, all of the information which they

would have needed to make what to them would be a commercially viable offer to the receiver. I think that an offering memorandum was of no commercial consequence to them, but the absence of one has since become a valuable tactical weapon.

57 It is my opinion that there is no convincing proof that if an offering memorandum had been widely distributed among persons qualified to have purchased Air Toronto, a viable offer would have come forth from a party other than 922 or OEL. Therefore, the failure to provide an offering memorandum was neither unfair, nor did it prejudice the obtaining of a better price on March 8, 1991, than that contained in the OEL offer. I would not give effect to the contention that the process adopted by the receiver was an unfair one.

58 There are two statements by Anderson J. contained in *Crown Trust Co. v. Rosenberg*, supra, which I adopt as my own. The first is at p. 109 [O.R.]:

> The court should not proceed against the recommendations of its Receiver except in special circumstances and where the necessity and propriety of doing so are plain. Any other rule or approach would emasculate the role of the Receiver and make it almost inevitable that the final negotiation of every sale would take place on the motion for approval.

The second is at p. 111 [O.R.]:

> It is equally clear, in my view, though perhaps not so clearly enunciated, that it is only in an exceptional case that the court will intervene and proceed contrary to the Receiver's recommendations if satisfied, as I am, that the Receiver has acted reasonably, prudently and fairly and not arbitrarily.

In this case the receiver acted reasonably, prudently, fairly and not arbitrarily. I am of the opinion, therefore, that the process adopted by the receiver in reaching an agreement was a just one.

59 In his reasons for judgment, after discussing the circumstances leading to the 922 offer, Rosenberg J. said this:

> They created a situation as of March 8th, where the Receiver was faced with two offers, one of which was in acceptable form and one of which could not possibly be accepted in its present form. The Receiver acted appropriately in accepting the OEL offer.

I agree.

60 The receiver made proper and sufficient efforts to get the best price that it could for the assets of Air Toronto. It adopted a reasonable and effective process to sell the airline which was fair to all persons who might be interested in purchasing it. It is my opinion, therefore, that the receiver properly carried out the mandate which was given to it by the order of O'Brien J. It follows that Rosenberg J. was correct when he confirmed the sale to OEL.

II. The effect of the support of the 922 offer by the two secured creditors.

61 As I noted earlier, the 922 offer was supported before Rosenberg J., and in this court, by CCFL and by the Royal Bank, the two secured creditors. It was argued that, because the interests of the creditors are primary, the

court ought to give effect to their wish that the 922 offer be accepted. I would not accede to that suggestion for two reasons.

62 The first reason is related to the fact that the creditors chose to have a receiver appointed by the court. It was open to them to appoint a private receiver pursuant to the authority of their security documents. Had they done so, then they would have had control of the process and could have sold Air Toronto to whom they wished. However, acting privately and controlling the process involves some risks. The appointment of a receiver by the court insulates the creditors from those risks. But, insulation from those risks carries with it the loss of control over the process of disposition of the assets. As I have attempted to explain in these reasons, when a receiver's sale is before the court for confirmation, the only issues are the propriety of the conduct of the receiver and whether it acted providently. The function of the court at that stage is not to step in and do the receiver's work, or change the sale strategy adopted by the receiver. Creditors who asked the court to appoint a receiver to dispose of assets should not be allowed to take over control of the process by the simple expedient of supporting another purchaser if they do not agree with the sale made by the receiver. That would take away all respect for the process of sale by a court-appointed receiver.

63 There can be no doubt that the interests of the creditor are an important consideration in determining whether the receiver has properly conducted a sale. The opinion of the creditors as to which offer ought to be accepted is something to be taken into account. But if the court decides that the receiver has acted properly and providently, those views are not necessarily determinative. Because, in this case, the receiver acted properly and providently, I do not think that the views of the creditors should override the considered judgment of the receiv- er.

64 The second reason is that, in the particular circumstances of this case, I do not think the support of CCFL and the Royal Bank of the 922 offer is entitled to any weight. The support given by CCFL can be dealt with summarily. It is a co-owner of 922. It is hardly surprising and not very impressive to hear that it supports the offer which it is making for the debtor's assets.

65 The support by the Royal Bank requires more consideration and involves some reference to the circumstances. On March 6, 1991, when the first 922 offer was made, there was in existence an inter-lender agreement between the Royal Bank and CCFL. That agreement dealt with the share of the proceeds of the sale of Air Toronto which each creditor would receive. At the time, a dispute between the Royal Bank and CCFL about the interpretation of that agreement was pending in the courts. The unacceptable condition in the first 922 offer related to the settlement of the inter-lender dispute. The condition required that the dispute be resolved in a way which would substantially favour CCFL. It required that CCFL receive $3,375,000 of the $6 million cash payment and the balance, including the royalties, if any, be paid to the Royal Bank. The Royal Bank did not agree with that split of the sale proceeds.

66 On April 5, 1991, the Royal Bank and CCFL agreed to settle the inter-lender dispute. The settlement was that if the 922 offer was accepted by the court, CCFL would receive only $1 million, and the Royal Bank would receive $5 million plus any royalties which might be paid. It was only in consideration of that settlement that the Royal Bank agreed to support the 922 offer.

67 The Royal Bank's support of the 922 offer is so affected by the very substantial benefit which it wanted to obtain from the settlement of the inter-lender dispute that, in my opinion, its support is devoid of any objectivity.

I think it has no weight.

68 While there may be circumstances where the unanimous support by the creditors of a particular offer could conceivably override the proper and provident conduct of a sale by a receiver, I do not think that this is such a case. This is a case where the receiver has acted properly and in a provident way. It would make a mockery out of the judicial process, under which a mandate was given to this receiver to sell this airline if the support by these creditors of the 922 offer were permitted to carry the day. I give no weight to the support which they give to the 922 offer.

69 In its factum, the receiver pointed out that, because of greater liabilities imposed upon private receivers by various statutes such as the *Employment Standards Act*, R.S.O. 1980, c. 137, and the *Environmental Protection Act*, R.S.O. 1980, c. 141, it is likely that more and more the courts will be asked to appoint receivers in insolvencies. In those circumstances, I think that creditors who ask for court-appointed receivers and business people who choose to deal with those receivers should know that if those receivers act properly and providently, their decisions and judgments will be given great weight by the courts who appoint them. I have decided this appeal in the way I have in order to assure business people who deal with court-appointed receivers that they can have confidence that an agreement which they make with a court-appointed receiver will be far more than a platform upon which others may bargain at the court approval stage. I think that persons who enter into agreements with court-appointed receivers, following a disposition procedure that is appropriate given the nature of the assets involved, should expect that their bargain will be confirmed by the court.

70 The process is very important. It should be carefully protected so that the ability of court-appointed receivers to negotiate the best price possible is strengthened and supported. Because this receiver acted properly and providently in entering into the OEL agreement, I am of the opinion that Rosenberg J. was right when he approved the sale to OEL and dismissed the motion to approve the 922 offer.

71 I would, accordingly, dismiss the appeal. I would award the receiver, OEL and Frontier Airlines Limited their costs out of the Soundair estate, those of the receiver on a solicitor-client scale. I would make no order as to the costs of any of the other parties or intervenors.

McKinlay J.A.:

72 I agree with Galligan J.A. in result, but wish to emphasize that I do so on the basis that the undertaking being sold in this case was of a very special and unusual nature. It is most important that the integrity of procedures followed by court-appointed receivers be protected in the interests of both commercial morality and the future confidence of business persons in their dealings with receivers. Consequently, in all cases, the court should carefully scrutinize the procedure followed by the receiver to determine whether it satisfies the tests set out by Anderson J. in *Crown Trust Co. v. Rosenberg* (1986), 67 C.B.R. (N.S.) 320n, 60 O.R. (2d) 87, 22 C.P.C. (2d) 131, 39 D.L.R. (4th) 526 (H.C.). While the procedure carried out by the receiver in this case, as described by Galligan J.A., was appropriate, given the unfolding of events and the unique nature of the assets involved, it is not a procedure that is likely to be appropriate in many receivership sales.

73 I should like to add that where there is a small number of creditors who are the only parties with a real interest in the proceeds of the sale (i.e., where it is clear that the highest price attainable would result in recovery so low that no other creditors, shareholders, guarantors, etc., could possibly benefit therefore), the wishes of the

interested creditors should be very seriously considered by the receiver. It is true, as Galligan J.A. points out, that in seeking the court appointment of a receiver, the moving parties also seek the protection of the court in carrying out the receiver's functions. However, it is also true that in utilizing the court process, the moving parties have opened the whole process to detailed scrutiny by all involved, and have probably added significantly to their costs and consequent shortfall as a result of so doing. The adoption of the court process should in no way diminish the rights of any party, and most certainly not the rights of the only parties with a real interest. Where a receiver asks for court approval of a sale which is opposed by the only parties in interest, the court should scrutinize with great care the procedure followed by the receiver. I agree with Galligan J.A. that in this case that was done. I am satisfied that the rights of all parties were properly considered by the receiver, by the learned motions court judge, and by Galligan J.A.

***Goodman J.A.* (dissenting):**

74 I have had the opportunity of reading the reasons for judgment herein of Galligan and McKinlay JJ.A. Respectfully, I am unable to agree with their conclusion.

75 The case at bar is an exceptional one in the sense that upon the application made for approval of the sale of the assets of Air Toronto, two competing offers were placed before Rosenberg J. Those two offers were that of OEL and that of 922, a company incorporated for the purpose of acquiring Air Toronto. Its shares were owned equally by CCFL and Air Canada. It was conceded by all parties to these proceedings that the only persons who had any interest in the proceeds of the sale were two secured creditors, viz., CCFL and the Royal Bank of Canada. Those two creditors were unanimous in their position that they desired the court to approve the sale to 922. We were not referred to, nor am I aware of, any case where a court has refused to abide by the unanimous wishes of the only interested creditors for the approval of a specific offer made in receivership proceedings.

76 In *British Columbia Developments Corp. v. Spun Cast Industries Ltd.* (1977), 26 C.B.R. (N.S.) 28, 5 B.C.L.R. 94 (S.C.), Berger J. said at p. 30 [C.B.R.]:

> Here all of those with a financial stake in the plant have joined in seeking the court's approval of the sale to Fincas. This court does not have a roving commission to decide what is best for investors and businessmen when they have agreed among themselves what course of action they should follow. It is their money.

77 I agree with that statement. It is particularly apt to this case. The two secured creditors will suffer a shortfall of approximately $50 million. They have a tremendous interest in the sale of assets which form part of their security. I agree with the finding of Rosenberg J. that the offer of 922 is superior to that of OEL. He concluded that the 922 offer is marginally superior. If by that he meant that mathematically it was likely to provide slightly more in the way of proceeds, it is difficult to take issue with that finding. If, on the other hand, he meant that having regard to all considerations it was only marginally superior, I cannot agree. He said in his reasons:

> I have come to the conclusion that knowledgeable creditors such as the Royal Bank would prefer the 922 offer even if the other factors influencing their decision were not present. No matter what adjustments had to be made, the 922 offer results in more cash immediately. Creditors facing the type of loss the Royal Bank is taking in this case would not be anxious to rely on contingencies especially in the present circumstances surrounding the airline industry.

78 I agree with that statement completely. It is apparent that the difference between the two offers insofar as cash on closing is concerned amounts to approximately $3 million to $4 million. The bank submitted that it did not wish to gamble any further with respect to its investment, and that the acceptance and court approval of the OEL offer in effect supplanted its position as a secured creditor with respect to the amount owing over and above the down payment and placed it in the position of a joint entrepreneur, but one with no control. This results from the fact that the OEL offer did not provide for any security for any funds which might be forthcoming over and above the initial down payment on closing.

79 In *Cameron v. Bank of Nova Scotia* (1981), 38 C.B.R. (N.S.) 1, 45 N.S.R. (2d) 303, 86 A.P.R. 303 (C.A.), Hart J.A., speaking for the majority of the court, said at p. 10 [C.B.R.]:

> Here we are dealing with a receiver appointed at the instance of one major creditor, who chose to insert in the contract of sale a provision making it subject to the approval of the court. This, in my opinion, shows an intention on behalf of the parties to invoke the normal equitable doctrines which place the court in the position of looking to the interests of all persons concerned before giving its blessing to a particular transaction submitted for approval. In these circumstances the court would not consider itself bound by the contract entered into in good faith by the receiver but would have to look to the broader picture to see that that contract was for the benefit of the creditors as a whole. When there was evidence that a higher price was readily available for the property the chambers judge was, in my opinion, justified in exercising his discretion as he did. Otherwise he could have deprived the creditors of a substantial sum of money.

80 This statement is apposite to the circumstances of the case at bar. I hasten to add that in my opinion it is not only price which is to be considered in the exercise of the judge's discretion. It may very well be, as I believe to be so in this case, that the amount of cash is the most important element in determining which of the two offers is for the benefit and in the best interest of the creditors.

81 It is my view, and the statement of Hart J.A. is consistent therewith, that the fact that a creditor has requested an order of the court appointing a receiver does not in any way diminish or derogate from his right to obtain the maximum benefit to be derived from any disposition of the debtor's assets. I agree completely with the views expressed by McKinlay J.A. in that regard in her reasons.

82 It is my further view that any negotiations which took place between the only two interested creditors in deciding to support the approval of the 922 offer were not relevant to the determination by the presiding judge of the issues involved in the motion for approval of either one of the two offers, nor are they relevant in determining the outcome of this appeal. It is sufficient that the two creditors have decided unanimously what is in their best interest, and the appeal must be considered in the light of that decision. It so happens, however, that there is ample evidence to support their conclusion that the approval of the 922 offer is in their best interests.

83 I am satisfied that the interests of the creditors are the prime consideration for both the receiver and the court. In *Re Beauty Counsellors of Canada Ltd.* (1986), 58 C.B.R. (N.S.) 237 (Ont. S.C.), Saunders J. said at p. 243:

> This does not mean that a court should ignore a new and higher bid made after acceptance where there has been no unfairness in the process. The interests of the creditors, while not the only consideration,

> are the prime consideration.

84 I agree with that statement of the law. In *Re Selkirk* (1986), 58 C.B.R. (N.S.) 245 (Ont. S.C.), Saunders J. heard an application for court approval of the sale by the sheriff of real property in bankruptcy proceedings. The sheriff had been previously ordered to list the property for sale subject to approval of the court. Saunders J. said at p. 246:

> In dealing with the request for approval, the court has to be concerned primarily with protecting the interests of the creditors of the former bankrupt. A secondary but important consideration is that the process under which the sale agreement is arrived at should be consistent with commercial efficacy and integrity.

85 I am in agreement with that statement as a matter of general principle. Saunders J. further stated that he adopted the principles stated by Macdonald J.A. in *Cameron*, supra, quoted by Galligan J.A. in his reasons. In *Cameron*, the remarks of Macdonald J.A. related to situations involving the calling of bids and fixing a time limit for the making of such bids. In those circumstances the process is so clear as a matter of commercial practice that an interference by the court in such process might have a deleterious effect on the efficacy of receivership proceedings in other cases. But Macdonald J.A. recognized that even in bid or tender cases where the offeror for whose bid approval is sought has complied with all requirements, a court might not approve the agreement of purchase and sale entered into by the receiver. He said at pp. 11-12 [C.B.R.]:

> There are, of course, many reasons why a court might not approve an agreement of purchase and sale, viz., where the offer accepted is so low in relation to the appraised value as to be unrealistic; or, where the circumstances indicate that insufficient time was allowed for the making of bids or that inadequate notice of sale by bid was given (where the receiver sells property by the bid method); or, where it can be said that the proposed sale is not in the best interest of either the creditors or the owner. Court approval must involve the delicate balancing of competing interests and not simply a consideration of the interests of the creditors.

86 The deficiency in the present case is so large that there has been no suggestion of a competing interest between the owner and the creditors.

87 I agree that the same reasoning may apply to a negotiation process leading to a private sale, but the procedure and process applicable to private sales of a wide variety of businesses and undertakings with the multiplicity of individual considerations applicable and perhaps peculiar to the particular business is not so clearly established that a departure by the court from the process adopted by the receiver in a particular case will result in commercial chaos to the detriment of future receivership proceedings. Each case must be decided on its own merits, and it is necessary to consider the process used by the receiver in the present proceedings and to determine whether it was unfair, improvident or inadequate.

88 It is important to note at the outset that Rosenberg J. made the following statement in his reasons:

> On March 8, 1991 the trustee accepted the OEL offer subject to court approval. The Receiver at that time had no other offer before it that was in final form or could possibly be accepted. The Receiver had at the time the knowledge that Air Canada with CCFL had not bargained in good faith and had not ful-

filled the promise of its letter of March 1st. The Receiver was justified in assuming that Air Canada and CCFL's offer was a long way from being in an acceptable form and that Air Canada and CCFL's objective was to interrupt the finalizing of the OEL agreement and to retain as long as possible the Air Toronto connector traffic flowing into Terminal 2 for the benefit of Air Canada.

89 In my opinion there was no evidence before him or before this court to indicate that Air Canada, with CCFL, had not bargained in good faith, and that the receiver had knowledge of such lack of good faith. Indeed, on his appeal, counsel for the receiver stated that he was not alleging Air Canada and CCFL had not bargained in good faith. Air Canada had frankly stated at the time that it had made its offer to purchase, which was eventually refused by the receiver, that it would not become involved in an "auction" to purchase the undertaking of Air Canada and that, although it would fulfil its contractual obligations to provide connecting services to Air Toronto, it would do no more than it was legally required to do insofar as facilitating the purchase of Air Toronto by any other person. In so doing, Air Canada may have been playing "hardball," as its behaviour was characterized by some of the counsel for opposing parties. It was nevertheless merely openly asserting its legal position, as it was entitled to do.

90 Furthermore, there was no evidence before Rosenberg J. or this court that the receiver had assumed that Air Canada and CCFL's objective in making an offer was to interrupt the finalizing of the OEL agreement and to retain as long as possible the Air Toronto connector traffic flowing into Terminal 2 for the benefit of Air Canada. Indeed, there was no evidence to support such an assumption in any event, although it is clear that 922, and through it CCFL and Air Canada, were endeavouring to present an offer to purchase which would be accepted and/or approved by the court in preference to the offer made by OEL.

91 To the extent that approval of the OEL agreement by Rosenberg J. was based on the alleged lack of good faith in bargaining and improper motivation with respect to connector traffic on the part of Air Canada and CCFL, it cannot be supported.

92 I would also point out that rather than saying there was no other offer before it that was final in form, it would have been more accurate to have said that there was *no unconditional* offer before it.

93 In considering the material and evidence placed before the court, I am satisfied that the receiver was at all times acting in good faith. I have reached the conclusion, however, that the process which he used was unfair insofar as 922 is concerned, and improvident insofar as the two secured creditors are concerned.

94 Air Canada had been negotiating with Soundair Corporation for the purchase from it of Air Toronto for a considerable period of time prior to the appointment of a receiver by the court. It had given a letter of intent indicating a prospective sale price of $18 million. After the appointment of the receiver, by agreement dated April 30, 1990, Air Canada continued its negotiations for the purchase of Air Toronto with the receiver. Although this agreement contained a clause which provided that the receiver "shall not negotiate for the sale ... of Air Toronto with any person except Air Canada," it further provided that the receiver would not be in breach of that provision merely by receiving unsolicited offers for all or any of the assets of Air Toronto. In addition, the agreement, which had a term commencing on April 30, 1990, could be terminated on the fifth business day following the delivery of a written notice of termination by one party to the other. I point out this provision merely to indicate that the exclusivity privilege extended by the receiver to Air Canada was of short duration at the receiver's op- tion.

95 As a result of due negligence investigations carried out by Air Canada during the months of April, May and June of 1990, Air Canada reduced its offer to $8.1 million conditional upon there being $4 million in tangible assets. The offer was made on June 14, 1990, and was open for acceptance until June 29, 1990.

96 By amending agreement dated June 19, 1990, the receiver was released from its covenant to refrain from negotiating for the sale of the Air Toronto business and assets to any person other than Air Canada. By virtue of this amending agreement, the receiver had put itself in the position of having a firm offer in hand, with the right to negotiate and accept offers from other persons. Air Canada, in these circumstances, was in the subservient position. The receiver, in the exercise of its judgment and discretion, allowed the Air Canada offer to lapse. On July 20, 1990, Air Canada served a notice of termination of the April 30, 1990 agreement.

97 Apparently as a result of advice received from the receiver to the effect that the receiver intended to conduct an auction for the sale of the assets and business of the Air Toronto division of Soundair Corporation, the solicitors for Air Canada advised the receiver by letter dated July 20, 1990, in part as follows:

> Air Canada has instructed us to advise you that it does not intend to submit a further offer in the auction process.

98 This statement, together with other statements set forth in the letter, was sufficient to indicate that Air Canada was not interested in purchasing Air Toronto in the process apparently contemplated by the receiver at that time. It did not form a proper foundation for the receiver to conclude that there was no realistic possibility of selling Air Toronto [to] Air Canada, either alone or in conjunction with some other person, in different circumstances. In June 1990, the receiver was of the opinion that the fair value of Air Toronto was between $10 million and $12 million.

99 In August 1990, the receiver contacted a number of interested parties. A number of offers were received which were not deemed to be satisfactory. One such offer, received on August 20, 1990, came as a joint offer from OEL and Air Ontario (an Air Canada connector). It was for the sum of $3 million for the good will relating to certain Air Toronto routes, but did not include the purchase of any tangible assets or leasehold interests.

100 In December 1990, the receiver was approached by the management of Canadian Partner (operated by OEL) for the purpose of evaluating the benefits of an amalgamated Air Toronto/Air Partner operation. The negotiations continued from December of 1990 to February of 1991, culminating in the OEL agreement dated March 8, 1991.

101 On or before December 1990, CCFL advised the receiver that it intended to make a bid for the Air Toronto assets. The receiver, in August of 1990, for the purpose of facilitating the sale of Air Toronto assets, commenced the preparation of an operating memorandum. He prepared no less than six draft operating memoranda with dates from October 1990 through March 1, 1991. None of these were distributed to any prospective bidder despite requests having been received therefor, with the exception of an early draft provided to CCFL without the receiver's knowledge.

102 During the period December 1990 to the end of January 1991, the receiver advised CCFL that the offering memorandum was in the process of being prepared and would be ready soon for distribution. He further advised CCFL that it should await the receipt of the memorandum before submitting a formal offer to purchase the

Air Toronto assets.

103 By late January, CCFL had become aware that the receiver was negotiating with OEL for the sale of Air Toronto. In fact, on February 11, 1991, the receiver signed a letter of intent with OEL wherein it had specifically agreed not to negotiate with any other potential bidders or solicit any offers from others.

104 By letter dated February 25, 1991, the solicitors for CCFL made a written request to the receiver for the offering memorandum. The receiver did not reply to the letter because he felt he was precluded from so doing by the provisions of the letter of intent dated February 11, 1991. Other prospective purchasers were also unsuccessful in obtaining the promised memorandum to assist them in preparing their bids. It should be noted that, exclusivity provision of the letter of intent expired on February 20, 1991. This provision was extended on three occasions, viz., February 19, 22 and March 5, 1991. It is clear that from a legal standpoint the receiver, by refusing to extend the time, could have dealt with other prospective purchasers, and specifically with 922.

105 It was not until March 1, 1991, that CCFL had obtained sufficient information to enable it to make a bid through 922. It succeeded in so doing through its own efforts through sources other than the receiver. By that time the receiver had already entered into the letter of intent with OEL. Notwithstanding the fact that the receiver knew since December of 1990 that CCFL wished to make a bid for the assets of Air Toronto (and there is no evidence to suggest that at that time such a bid would be in conjunction with Air Canada or that Air Canada was in any way connected with CCFL), it took no steps to provide CCFL with information necessary to enable it to make an intelligent bid, and indeed suggested delaying the making of the bid until an offering memorandum had been prepared and provided. In the meantime, by entering into the letter of intent with OEL, it put itself in a position where it could not negotiate with CCFL or provide the information requested.

106 On February 28, 1991, the solicitors for CCFL telephoned the receiver and were advised for the first time that the receiver had made a business decision to negotiate solely with OEL and would not negotiate with anyone else in the interim.

107 By letter dated March 1, 1991, CCFL advised the receiver that it intended to submit a bid. It set forth the essential terms of the bid and stated that it would be subject to customary commercial provisions. On March 7, 1991 CCFL and Air Canada, jointly through 922, submitted an offer to purchase Air Toronto upon the terms set forth in the letter dated March 1, 1991. It included a provision that the offer was conditional upon the interpretation of an inter-lender agreement which set out the relative distribution of proceeds as between CCFL and the Royal Bank. It is common ground that it was a condition over which the receiver had no control, and accordingly would not have been acceptable on that ground alone. The receiver did not, however, contact CCFL in order to negotiate or request the removal of the condition, although it appears that its agreement with OEL not to negotiate with any person other than OEL expired on March 6, 1991.

108 The fact of the matter is that by March 7, 1991, the receiver had received the offer from OEL which was subsequently approved by Rosenberg J. That offer was accepted by the receiver on March 8, 1991. Notwithstanding the fact that OEL had been negotiating the purchase for a period of approximately 3 months, the offer contained a provision for the sole benefit of the purchaser that it was subject to the purchaser obtaining "a financing commitment within 45 days of the date hereof in an amount not less than the Purchase Price from the Royal Bank of Canada or other financial institution upon terms and conditions acceptable to them. In the event that such a financing commitment is not obtained within such 45 day period, the purchaser or OEL shall have the

right to terminate this agreement upon giving written notice of termination to the vendor on the first Business Day following the expiry of the said period." The purchaser was also given the right to waive the condition.

109 In effect, the agreement was tantamount to a 45-day option to purchase, excluding the right of any other person to purchase Air Toronto during that period of time and thereafter if the condition was fulfilled or waived. The agreement was, of course, stated to be subject to court approval.

110 In my opinion, the process and procedure adopted by the receiver was unfair to CCFL. Although it was aware from December 1990 that CCFL was interested in making an offer, it effectively delayed the making of such offer by continually referring to the preparation of the offering memorandum. It did not endeavour during the period December 1990 to March 7, 1991, to negotiate with CCFL in any way the possible terms of purchase and sale agreement. In the result, no offer was sought from CCFL by the receiver prior to February 11, 1991, and thereafter it put itself in the position of being unable to negotiate with anyone other than OEL. The receiver then, on March 8, 1991, chose to accept an offer which was conditional in nature without prior consultation with CCFL (922) to see whether it was prepared to remove the condition in its offer.

111 I do not doubt that the receiver felt that it was more likely that the condition in the OEL offer would be fulfilled than the condition in the 922 offer. It may be that the receiver, having negotiated for a period of 3 months with OEL, was fearful that it might lose the offer if OEL discovered that it was negotiating with another person. Nevertheless, it seems to me that it was imprudent and unfair on the part of the receiver to ignore an offer from an interested party which offered approximately triple the cash down payment without giving a chance to the offeror to remove the conditions or other terms which made the offer unacceptable to it. The potential loss was that of an agreement which amounted to little more than an option in favour of the offeror.

112 In my opinion the procedure adopted by the receiver was unfair to CCFL in that, in effect, it gave OEL the opportunity of engaging in exclusive negotiations for a period of 3 months, notwithstanding the fact that it knew CCFL was interested in making an offer. The receiver did not indicate a deadline by which offers were to be submitted, and it did not at any time indicate the structure or nature of an offer which might be acceptable to it.

113 In his reasons, Rosenberg J. stated that as of March 1, CCFL and Air Canada had all the information that they needed, and any allegations of unfairness in the negotiating process by the receiver had disappeared. He said:

> They created a situation as of March 8, where the receiver was faced with two offers, one of which was acceptable in form and one of which could not possibly be accepted in its present form. The Receiver acted appropriately in accepting the OEL offer.

If he meant by "acceptable in form" that it was acceptable to the receiver, then obviously OEL had the unfair advantage of its lengthy negotiations with the receiver to ascertain what kind of an offer would be acceptable to the receiver. If, on the other hand, he meant that the 922 offer was unacceptable in its form because it was conditional, it can hardly be said that the OEL offer was more acceptable in this regard, as it contained a condition with respect to financing terms and conditions "*acceptable to them*."

114 It should be noted that on March 13, 1991, the representatives of 922 first met with the receiver to review

its offer of March 7, 1991, and at the request of the receiver, withdrew the inter-lender condition from its offer. On March 14, 1991, OEL removed the financing condition from its offer. By order of Rosenberg J. dated March 26, 1991, CCFL was given until April 5, 1991, to submit a bid, and on April 5, 1991, 922 submitted its offer with the inter-lender condition removed.

115 In my opinion, the offer accepted by the receiver is improvident and unfair insofar as the two creditors are concerned. It is not improvident in the sense that the price offered by 922 greatly exceeded that offered by OEL. In the final analysis it may not be greater at all. The salient fact is that the cash down payment in the 922 offer constitutes proximately two thirds of the contemplated sale price, whereas the cash down payment in the OEL transaction constitutes approximately 20 to 25 per cent of the contemplated sale price. In terms of absolute dollars, the down payment in the 922 offer would likely exceed that provided for in the OEL agreement by approximately $3 million to $4 million.

116 In *Re Beauty Counsellors of Canada Ltd.*, supra, Saunders J. said at p. 243 [C.B.R.]:

> If a substantially higher bid turns up at the approval stage, the court should consider it. Such a bid may indicate, for example, that the trustee has not properly carried out its duty to endeavour to obtain the best price for the estate. In such a case the proper course might be to refuse approval and to ask the trustee to recommence the process.

117 I accept that statement as being an accurate statement of the law. I would add, however, as previously indicated, that in determining what is the best price for the estate, the receiver or court should not limit its consideration to which offer provides for the greater sale price. The amount of down payment and the provision or lack thereof to secure payment of the balance of the purchase price over and above the down payment may be the most important factor to be considered, and I am of the view that is so in the present case. It is clear that that was the view of the only creditors who can benefit from the sale of Air Toronto.

118 I note that in the case at bar the 922 offer in conditional form was presented to the receiver before it accepted the OEL offer. The receiver, in good faith, although I believe mistakenly, decided that the OEL offer was the better offer. At that time the receiver did not have the benefit of the views of the two secured creditors in that regard. At the time of the application for approval before Rosenberg J., the stated preference of the two interested creditors was made quite clear. He found as fact that knowledgeable creditors would not be anxious to rely on contingencies in the present circumstances surrounding the airline industry. It is reasonable to expect that a receiver would be no less knowledgeable in that regard, and it is his primary duty to protect the interests of the creditors. In my view, it was an improvident act on the part of the receiver to have accepted the conditional offer made by OEL, and Rosenberg J. erred in failing to dismiss the application of the receiver for approval of the OEL offer. It would be most inequitable to foist upon the two creditors, who have already been seriously hurt, more unnecessary contingencies.

119 Although in other circumstances it might be appropriate to ask the receiver to recommence the process, in my opinion, it would not be appropriate to do so in this case. The only two interested creditors support the acceptance of the 922 offer, and the court should so order.

120 Although I would be prepared to dispose of the case on the grounds stated above, some comment should be addressed to the question of interference by the court with the process and procedure adopted by the receiver.

121 I am in agreement with the view expressed by McKinlay J.A. in her reasons that the undertaking being sold in this case was of a very special and unusual nature. As a result, the procedure adopted by the receiver was somewhat unusual. At the outset, in accordance with the terms of the receiving order, it dealt solely with Air Canada. It then appears that the receiver contemplated a sale of the assets by way of auction, and still later contemplated the preparation and distribution of an offering memorandum inviting bids. At some point, without advice to CCFL, it abandoned that idea and reverted to exclusive negotiations with one interested party. This entire process is not one which is customary or widely accepted as a general practice in the commercial world. It was somewhat unique, having regard to the circumstances of this case. In my opinion, the refusal of the court to approve the offer accepted by the receiver would not reflect on the integrity of procedures followed by court-appointed receivers, and is not the type of refusal which will have a tendency to undermine the future confidence of business persons in dealing with receivers.

122 Rosenberg J. stated that the Royal Bank was aware of the process used and tacitly approved it. He said it knew the terms of the letter of intent in February 1991, and made no comment. The Royal Bank did, however, indicate to the receiver that it was not satisfied with the contemplated price, nor the amount of the down payment. It did not, however, tell the receiver to adopt a different process in endeavouring to sell the Air Toronto assets. It is not clear from the material filed that at the time it became aware of the letter of intent that it knew that CCFI was interested in purchasing Air Toronto.

123 I am further of the opinion that a prospective purchaser who has been given an opportunity to engage in exclusive negotiations with a receiver for relatively short periods of time which are extended from time to time by the receiver, and who then makes a conditional offer, the condition of which is for his sole benefit and must be fulfilled to his satisfaction unless waived by him, and which he knows is to be subject to court approval, cannot legitimately claim to have been unfairly dealt with if the court refuses to approve the offer and approves a substantially better one.

124 In conclusion, I feel that I must comment on the statement made by Galligan J.A. in his reasons to the effect that the suggestion made by counsel for 922 constitutes evidence of lack of prejudice resulting from the absence of an offering memorandum. It should be pointed out that the court invited counsel to indicate the manner in which the problem should be resolved in the event that the court concluded that the order approving the OEL offer should be set aside. There was no evidence before the court with respect to what additional information may have been acquired by CCFL since March 8, 1991, and no inquiry was made in that regard. Accordingly, I am of the view that no adverse inference should be drawn from the proposal made as a result of the court's invitation.

125 For the above reasons I would allow the appeal one set of costs to CCFL-922, set aside the order of Rosenberg J., dismiss the receiver's motion with one set of costs to CCFL-922 and order that the assets of Air Toronto be sold to numbered corporation 922246 on the terms set forth in its offer with appropriate adjustments to provide for the delay in its execution. Costs awarded shall be payable out of the estate of Soundair Corporation. The costs incurred by the receiver in making the application and responding to the appeal shall be paid to him out of the assets of the estate of Soundair Corporation on a solicitor-client basis. I would make no order as to costs of any of the other parties or intervenors.

Appeal dismissed.

7 C.B.R. (3d) 1, 4 O.R. (3d) 1, 83 D.L.R. (4th) 76, 46 O.A.C. 321

END OF DOCUMENT

TAB 5

2005 CarswellOnt 1240

Tiger Brand Knitting Co., Re
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: TIGER BRAND KNITTING COMPANY LIMITED (Applicants)
Ontario Superior Court of Justice
C. Campbell J.
Heard: April 1, 2005
Judgment: April 5, 2005
Docket: 04-CL-5532

Counsel: Scott A. Bomhof for Monitor RSM Richter Inc.

Orestes Pasparakis for GMAC Commercial Finance Corporation-Canada

Sean Dewart for USWA

Renée B. Brosseau for Tiger Brand Knitting Company Limited

Steven L. Gaff for Geetext Global Sourcing Inc.

Christopher Besant for Joan Fisk

Fred Myers for Prospective Purchaser

Hugh Mackenzie for Andrew Warnock, James Warnock

Leonard Alksnis for Majority of the Members of the board

Subject: Insolvency; Estates and Trusts

Bankruptcy and insolvency --- Administration of estate -- Sale of assets -- Miscellaneous issues

Applicant applied for and received protection from its creditors under Companies' Creditors Arrangement Act -- Court ordered sale of assets rather than restructuring as asset sale was most likely result of ongoing efforts to maximize stakeholder returns -- G made offer to purchase applicant's assets, subject to deadline for receipt of superior offers -- Both trade union representing applicant's employees and major creditor believed superior offers were available and "break fee" was negotiated with G -- When deadline for other offers passed G took position its offer should be accepted or it should be paid "break fee" -- Monitor applied for extension of time to negotiate with potential purchasers -- Trade union applied for order that monitor be directed not to close deal with prospective purchaser and to negotiate with company which might preserve jobs of some of applicant's employees -- Application to extend time was granted; application by trade union was dismissed -- Court had jurisdiction to make order sought by trade union but it was not appropriate -- There was no suggestion that monitor had acted inappropriately or breached any of its obligations -- To allow offering process to be reopened by enjoining monitor from completing proposed transaction would amount to unfairness to prospective purchaser, to G, and to secured creditor.

Cases considered by C. Campbell J.:

Crown Trust Co. v. Rosenberg (1986), 60 O.R. (2d) 87, 22 C.P.C. (2d) 131, 39 D.L.R. (4th) 526, 67 C.B.R. (N.S.) 320 (note), 1986 CarswellOnt 235 (Ont. H.C.) -- followed

Royal Bank v. Soundair Corp. (1991), 7 C.B.R. (3d) 1, 83 D.L.R. (4th) 76, 46 O.A.C. 321, 4 O.R. (3d) 1, 1991 CarswellOnt 205 (Ont. C.A.) -- followed

Stelco Inc., Re (2005), 2005 CarswellOnt 1188 (Ont. C.A.) -- considered

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3

Generally -- referred to

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

Generally -- referred to

s. 11 -- referred to

APPLICATION by monitor for extension of time in which to negotiate with prospective purchaser; Application by trade union for order enjoining monitor from closing sale.

***C. Campbell J.*:**

1 Tiger Brand Knitting Company Limited ("the Applicant") and RSM Richter Inc. ("the Monitor") seek an extension of the time within which to present an offer to the Court for the sale of the business and assets of the Applicant.

2 The extension of up to 15 days is not opposed. Counsel on behalf of the United Steel Workers of America ("USWA") urges the Court to add a condition to the granting of any extension, namely, that the Monitor be directed not to accept a bid offer that it has received and to negotiate with another party that may make an offer.

3 USWA seeks to add the condition with the prospect that a new offer, if it comes forward, would provide the opportunity of some or all of the 200 jobs now occupied by its members at the Applicant's facility in Cambridge.

4 Very simply, it is urged that the broad considerations available to the Court to provide remedy under *The*

Companies' Creditors Arrangement Act ("CCAA") permit the Court to take into account and balance the interests of all stakeholders, not just those of a purchaser who would provide the greatest immediate monetary recovery to a secured creditor.

Background Facts

5 On August 30, 2004, the Applicant filed for, and obtained, protection from its creditors under the CCAA pursuant to the "Initial Order." The stay of proceedings was initially for a period of 30 days and since September 29, 2004, has been extended on a number of occasions, the last being March 15, 2005.

6 Tiger Brand, which is in the business of design and manufacture of casual clothing, has been subject to the impact of globalization, which has seen cheaper goods manufactured abroad displace domestic production. This, together with the rise of the Canadian dollar relative to the United States dollar, has resulted in a deterioration of financial performance.

7 The impact will particularly felt by the employees in head office and manufacturing facilities in Cambridge, Ontario, but as well by the Company's three retail outlets.

8 From the commencement of its involvement, the Monitor has recognized that a so-called multi-track process provided the only realistic opportunity to maximize stakeholder returns. As set out in the Monitor's First Report, these included (a) soliciting offers for the business and assets; (b) considering shareholders' restructuring plans; (c) the liquidation value of assets; and (d) assisting in identification of potential investors.

9 Subject to comments below, none of the interested parties has taken the position that the Monitor has not reasonably or appropriately carried out its duties in accordance with Court Orders.

10 By this Court's Order of September 13, 2004, a Sale Process was approved, as it was recognized that a sale of assets rather than a restructuring of the Company was the more likely result of the ongoing effort.

11 The marketing process was extended and by Order of November 3, 2004, amended as set out in that Order with the explanation and rationale for it contained in the Monitor's Fifth Report to the Court dated January 11, 2005:

- The Monitor originally identified a sale transaction with Geetex which, at the time, provided the highest value to the stakeholders and had the greatest probability of closing. Importantly, the Geetex offer was premised on an asset acquisition which would likely result in Geetex carrying on an importing operation; and, as such, an orderly wind-down and termination of the Company's manufacturing and possibly other operations in Cambridge, Ontario;

- Geetex agreed that its offer would be a "stalking horse" in the amended sale process. Parties interested in purchasing the Assets for an amount greater than the Geetex stalking horse bid had to submit offers by a November 12, 2004 deadline;

12 A deadline of November 12, 2004 was set for the receipt of offers pursuant to the Amended Sale Process, the short time period being considered necessary due to a belief by, among others, Geetex that, "if a transaction was not consummated in short order, the assets and the business of Tiger Brand generally would deteriorate sig-

nificantly and rapidly in value."

13 Apparently, both the major secured creditor GMAC and the Union were of the view that superior offers were available, the process was extended and in early January 2005, a "stay fee" was negotiated between the Monitor and Geetex, whereby Geetex kept its offer open to February 15, 2005.

14 Geetex takes the position that there has not been until most recently an offer superior to its and that either the new offer from a new purchaser of assets should be accepted and closed, or Geetex's offer accepted and completed, or it be paid the break fee plus costs.

15 As of the time of its Sixth Report, the Monitor had executed non-binding non-exclusive memoranda of understanding with two prospective purchasers and looked forward to one or both of the parties presenting a final form of asset purchase agreement for consideration.

16 Since that time, the Monitor has been negotiating an agreement with one prospective purchaser, which is expected to be finalized and executed shortly. Hence the request for an extension to April 15, 2005.

17 The affidavit material filed on behalf of USWA identifies a potential bidder, which, if successful, would provide the opportunity for preservation of some employment in Cambridge.

18 In effect, USWA complains that the Monitor will not now consider and negotiate an offer from this bidder, which effectively eliminates the possibility of saving employment in Cambridge.

19 The Monitor reports in its Seventh Report that efforts to identify going-concern purchasers that would preserve employment at Cambridge have been unsuccessful.

20 The position of the Monitor, supported by the major secured creditor, Geetex and the prospective purchaser, is that to add a condition to the grant of extension would undermine and violate the process that has been followed to date.

Analysis & Law

21 Two principles involving the Court's jurisdiction and discretion are urged, one by USWA and another by those who oppose an extension of the time to complete a plan on terms.

22 USWA submits that the broad discretion given to the Court to take into account the interests of all stakeholders not just secured creditors, directs that in these circumstances, every reasonable consideration be given to the saving of jobs and of the Company to operate as an entity.

23 Mr. Dewart submits that the broad and flexible discretion given to the Court under the CCAA favours any reasonable effort to preserve the business under a restructuring as opposed to a liquidation, which is more properly achieved under the BIA.

24 The balancing effort, it is suggested, should allow those stakeholders who wish to achieve continuance of the enterprise every reasonable opportunity to do so and in this case, the only way to do so is to require the Monitor to not accept an offer to purchase assets until it at least considers a bid from an entity that might allow

continuance of at least some of the business.

25 The Court of Appeal for Ontario rendered a decision on March 31, 2005 dealing with the issue of removal of directors in the context of a CCAA proceeding.

26 In *Stelco Inc., Re* [2005 CarswellOnt 1188 (Ont. C.A.)], the reasons of Blair J. for the Court considered the extent to which the Court's "inherent jurisdiction" and "discretion" under the CCAA might be involved to provide the remedy sought.

27 After adopting the observation from I.H. Jacob's "The Inherent Jurisdiction of the Court" (1970), 23 Current Legal Problems at p. 2, that there is a vital distinction between jurisdiction and discretion that must be observed, he went on to say at paragraph 38:

> [38] I do not mean to suggest that inherent jurisdiction can never apply in a CCAA context. The court retains the ability to control its own process, should the need arise. There is a distinction, however - difficult as it may be to draw -- between the *court's* process with respect to the restructuring, on the one hand, and the course of action involving the negotiations and corporate actions accompanying them, which are the *company's* process, on the other hand. The court simply supervises the latter process through its ability to stay, restrain or prohibit proceedings against the company during the plan negotiation period "on such terms as it may impose." Hence the better view is that a judge is generally exercising the court's statutory discretion under s. 11 of the Act when supervising a CCAA proceeding. [Footnote omitted]

28 At paragraph 39, in commenting on the discretion of a judge under s. 11 of the CCAA to, among other things, stay, restrain further proceedings or prohibit actions against the Company acting in good faith and with due diligence, Blair J.A. went on to say:

> In my view, the s. 11 discretion -- in spite of its considerable breadth and flexibility -- does not permit the exercise of such a power in and of itself.

29 Paragraph 44 reads:

> [44] What the court does under s. 11 is to establish the boundaries of the playing field and act as a referee in the process. The company's role in the restructuring, and that of its stakeholders, is to work out a plan or compromise that a sufficient percentage of creditors will accept and the court will approve and sanction. The corporate activities that take place in the course of the workout are governed by the legislation and legal principles that normally apply to such activities. In the course of acting as referee, the court has great leeway, as Farley J. observed in *Lehndorff, supra*, at para 5, "to make order[s] so as to effectively maintain the status quo in respect of an insolvent company while it attempts to gain the approval of its creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors". But the s. 11 discretion is not open-ended and unfettered. Its exercise must be guided by the scheme and object of the Act and by the legal principles that govern corporate law issues. ...

30 This leads to the principle relied on by those who oppose the extension on conditions that would favour a

new offer.

31 The principle is that process that has been put in place for receiving offers in respect of either the business as a going concern or of its assets, should be honoured. The process is integral to the administration of statutes such as the BIA and the CCAA.

32 *Royal Bank v. Soundair Corp.* (1991), 7 C.B.R. (3d) 1 (Ont. C.A.) is a decision of the Court of Appeal for Ontario. At issue was the power of the Court to review a decision of a receiver to approve one offer over another for the sale of an airline as a going concern.

33 At paragraph 42, Galligan J.A. for the majority (himself and McKinlay J.A.) said:

> While it is accepted that the primary concern of a receiver is the protecting of the interests of the creditors, there is a secondary but very important consideration, and that is the integrity of the process by which the sale is effected.

34 At paragraph 16, the statement made by Anderson J. in *Crown Trust Co. v. Rosenberg* (1986), 60 O.R. (2d) 87 (Ont. H.C.) at p. 92 was adopted and the duties of the Court summarized as follows:

> 1. It should consider whether the receiver has made a sufficient effort to get the best price and has not acted improvidently.
>
> 2. It should consider the interests of all parties.
>
> 3. It should consider the efficacy and integrity of the process by which offers are obtained.
>
> 4. It should consider whether there has been unfairness in the working out of the process.

35 To my mind, those same duties of the Court are implicit in a marketing and sale process pursuant to Court Order under the CCAA.

36 There is nothing in the material before me or in the submissions of Mr. Dewart that suggest that any of those duties have to date been breached by the Monitor in the negotiation or offer process.

37 At this point in time, I am of the view that to allow the offering process to in effect be reopened by enjoining the Monitor from completing a proposed transaction would amount to an unfairness in the working out of the process to the prospective purchaser, to Geetex and to GMAC the secured creditor. As well, it would interfere with the efficacy and integrity of the process and prefer the interests of one party (the USWA, albeit an important one) over others. As noted at paragraph 46 of *Soundair*

> [46] It is my opinion that the court must exercise extreme caution before it interferes with the process adopted by a receiver to sell an unusual asset. It is important that prospective purchasers know that, if they are acting in good faith, bargain seriously with a receiver and enter into an agreement with it, a court will not lightly interfere with the commercial judgment of the receiver to sell the asset to them.

38 This is not to suggest that the interests urged by the USWA would be without remedy in appropriate cir-

cumstances.

39 The dissent of Goodman J.A. in *Soundair* was really on the factual side, as he concluded that in his view, the conditional offer accepted by the Receiver in that case was "...an improvident one..." [at paragraph 118.]

40 In this case, there is no accepted offer before the Court for approval. When there is, should there be another offer that would meet the test of rendering the accepted offer improvident, the Court can and perhaps should intervene.

41 Until that occurs, I do not conclude on the facts before me, that the Monitor has acted improvidently in failing to negotiate with a party who did not bring forward an offer capable of acceptance within the process set out in the previous Order of the Court. The actions of the Monitor appear entirely appropriate.

42 For the above reasons, the motion to extend the time within which to present an offer for sale of the business and assets of the Applicant is extended to April 15, 2005 or such earlier date as may be appropriate without the condition as sought by the USWA.

43 If it is necessary to deal with any issue of costs, they may be spoken to at a 9:30 appointment.

Application by monitor granted; application by trade union dis- missed.

END OF DOCUMENT

TAB 6

36 C.B.R. (5th) 296

2007 CarswellOnt 5799

Textron Financial Canada Ltd. v. Beta Ltée/Beta Brands Ltd.
Textron Financial Canada Limited (Applicant) and Beta Limitee/Beta Brands Limited (Respondent) and Bakery, Confectionery, Tobacco Workers and Grain Millers International Union, Local 242 and Mintz & Partners Limited and Capitalink, L.C.
Ontario Superior Court of Justice
L.C. Leitch R.S.J.
Heard: July 19, 2007
Judgment: August 1, 2007
Docket: 06-CL-6820

Counsel: E. Patrick Shea for Applicant, Textron Financial Canada Limited

Steven Weisz for Respondent, Sun Beta Brands

Duncan Grace for Moving Party, The Bakery, Confectionery, Tobacco Workers and Grain Millers International Union, Local 242

Jeffrey J. Simpson for Mintz & Partners Limited

Kenneth D. Kraft for Capitalink, L.C.

Frank A. Highley for Rob Neable, Gary Musick and Anita Varallo

Subject: Insolvency; Restitution; Corporate and Commercial

Bankruptcy and insolvency --- Priorities of claims -- Unsecured claims -- General principles

Creditor agreed in fall 2004 to market company's assets and property for sale for fee based on consideration received by company from transactions with party introduced by creditor -- Due to creditor's marketing efforts, R submitted purchase proposal in March 2006, and its subsidiary B executed asset purchase agreement on December 13, 2006 -- Receiver was appointed for company on January 3, 2007, and B sale was approved by court order -- Pursuant to contractual arrangements, creditor was entitled to $120,000 U.S. fee -- Receiver applied for advice and directions in respect of payment of fee claimed by creditor as result of successful completion by receiver of B transaction -- Receiver was not bound by agreement and was not obligated to pay creditor's fee -- Creditor's claim was unsecured and therefore retained no priority to payment within receivership scheme -- Agreement of purchase and sale was executed before receiver was appointed -- Receiver's reliance on creditor's marketing efforts after its appointment was conduct in accordance with its statutory obligation to act in commercially reasonable manner, but there was no evidence that receiver adopted or agreed to be personally bound by agreement -- Court order approving B transaction did not have effect of imposing personal liability on receiver for payment of commission under agreement.

Restitution and unjust enrichment --- Benefits conferred in anticipation of reward -- Quantum meruit

Creditor agreed in fall 2004 to market company's assets and property for sale for fee based on consideration received by company from transactions with party introduced by creditor -- Due to creditor's marketing efforts, R submitted purchase proposal in March 2006, and its subsidiary B executed asset purchase agreement on December 13, 2006 -- Receiver was appointed for company on January 3, 2007, and B sale was approved by court order -- Pursuant to contractual arrangements, creditor was entitled to $120,000 U.S. fee -- Receiver applied for advice and directions in respect of payment of fee claimed on quantum meruit basis -- Requirements for unjust enrichment and application of quantum meruit remedy were not established -- In relying on creditor's marketing efforts, receiver obtained benefit -- Receivership status of company meant that there was possibility that creditor would be deprived of payment, however, that deprivation did not correspond to conduct of receiver, but rather to financial status of company -- Efforts rendered by creditor did not create reasonable expectation that such were compensable by receiver -- Creditor's arrangement for payment extended only to company, and court order approving B transaction was insufficient to establish reasonable expectation that receiver should compensate creditor for its efforts -- There was no absence of juristic reason for enrichment, as receiver had obligation to deal with company's assets in commercially reasonable manner and in relying on creditor's marketing efforts, receiver was simply complying with that obligation.

Bankruptcy and insolvency --- Priorities of claims -- Preferred claims -- Wages and salaries of employees -- Priority over other creditors

KERP payments -- Company had seven senior management positions, but by fall 2006, only three remained -- Company gave key employees letters setting out severance arrangements including payments of $50,000 to $249,000 if they remained with company and employment was terminated without cause -- Key employees remained until their termination in January 2007 -- Receiver was appointed for company on January 3, 2007 -- Key employee retention payments ("KERP") arrangement was never solidified between parties, and receiver elected not to undertake to make KERP payments -- Employees alleged that secured creditors agreed that incentive payments totalling $166,000 would be included in cash flows related to B transaction to be paid on closing, which transaction was later approved by court -- Receiver applied for advice and directions in respect of KERP payments -- Payments should not be made -- Employees' efforts were aimed at completion of B transaction, and it was unclear whether services rendered went beyond their normal duties as salaried members of senior management -- Employees were attempting to "jump the queue" of unsecured creditors in advancing claim -- Payments sought appeared to be more in nature of severance payment than KERP payment -- Even if payments were properly characterized as KERP payments, they were not entitled to statutory priority or preference.

Cases considered by L.C. Leitch R.S.J.:

Armadale Properties Ltd. v. 700 King Street (1997) Ltd. (2001), 2001 CarswellOnt 1567, 25 C.B.R. (4th) 198 (Ont. S.C.J. [Commercial List]) -- considered

Aurora Development Ltd. v. Paradise (Town) (1991), 1991 CarswellNfld 261, 90 Nfld. & P.E.I.R. 5, 280 A.P.R. 5 (Nfld. T.D.) -- referred to

Consulate Ventures Inc. v. Amico Contracting & Engineering (1992) Inc. (2007), 2007 CarswellOnt 2627, 2007 ONCA 324, 223 O.A.C. 330 (Ont. C.A.) -- considered

Global Home Products, LLC, Re (2007), 369 B.R. 778, Bankr. L. Rep. P 81,001 (U.S. Bankr. D. Del.) -- considered

Hill v. Develcon Electronics Ltd. (1991), (sub nom. Hill v. Develcon Electronics Ltd. (No. 2)) 92 Sask. R. 258, 37 C.C.E.L. 42, 1991 CarswellSask 247 (Sask. Q.B.) -- referred to

Hoffer v. Verdone (1994), 1994 CarswellOnt 3268 (Ont. Gen. Div.) -- referred to

Honey-Bee Sanitation Inc. v. Essex (County) (1993), 1993 CarswellOnt 3091 (Ont. Gen. Div.) -- referred to

Howlett v. 512046 B.C. Ltd. (2000), 17 C.B.R. (4th) 224, 2000 BCSC 871, 2000 CarswellBC 1130 (B.C. S.C. [In Chambers]) -- referred to

Johnson v. H.G. Precision Machine Ltd. (April 5, 1991), Doc. New Westminster F891301 (B.C. S.C.) -- referred to

Panamericana de Bienes y Servicios S.A. v. Northern Badger Oil & Gas Ltd. (1991), 8 C.B.R. (3d) 31, 1991 CarswellAlta 315, 81 Alta. L.R. (2d) 45, [1991] 5 W.W.R. 577, 81 D.L.R. (4th) 280, 7 C.E.L.R. (N.S.) 66, 117 A.R. 44, 2 W.A.C. 44 (Alta. C.A.) -- considered

Ram Industrial Equipment (Toronto) Ltd. v. Kolson (1998), 115 O.A.C. 348, 1998 CarswellOnt 4304 (Ont. C.A.) -- considered

Rodaro v. Royal Bank (2002), 49 R.P.R. (3d) 227, 157 O.A.C. 203, 22 B.L.R. (3d) 274, 59 O.R. (3d) 74, 2002 CarswellOnt 1047 (Ont. C.A.) -- considered

Warehouse Drug Store Ltd., Re (2006), 24 C.B.R. (5th) 275, 2006 CarswellOnt 5128 (Ont. S.C.J.) -- distinguished

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3

Generally -- referred to

s. 14.06(1.2) [en. 1997, c. 12, s. 15(1)] -- considered

s. 75 -- referred to

s. 247 -- referred to

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

Generally -- referred to

APPLICATION by receiver for advice and directions in respect of certain payments.

L.C. Leitch R.S.J.:

1 Mintz & Partners Limited, (the "Receiver"), in its capacity as interim receiver and receiver of Beta Limited/ Beta Brands Limited, ("Beta Brands"), applies for advice and directions in respect of the following:

> (A) The payment by the Receiver of a fee (the "Capitalink Fee") of US$120,000 being claimed by Capitalink, L.C. ("Capitalink") as a result of the successful completion by the Receiver of a transaction (the "Bremner Transaction") to sell certain of the assets of Beta Brands to Bremner Food Group In. ("Bremner"); and
>
> (B) The payment of $198,000 by the Receiver in key employee retention payments (the "KERP Payments") representing payments in the amount of $66,000 each being claimed by Mr. Robert Neable, Mr. Gary Musick, and Ms. Anita Varallo.

Part (A): The Capitalink Fee

Background Facts

2 Capitalink became involved with Beta Brands in the fall of 2004. At that time, Beta Brands established an agreement with Capitalink (the "Capitalink Agreement") to, *inter alia*, market its assets and property for sale. Beta Brands was required to pay Capitalink a fee based on the consideration received by Beta Brands from any transaction with a party introduced to it by Capitalink.

3 Capitalink provided expert advice to Beta Brands from September 2005 to December 2006. It investigated several marketing options for Beta Brands and prepared information memoranda to be made available to prospective purchasers.

4 As a result of Capitalink's marketing efforts, Ralcorp Holdings submitted a purchase proposal in March 2006. Bremner, the subsidiary of Ralcorp, executed an Asset Purchase Agreement on December 13, 2006.

5 The Receiver was appointed interim receiver and receiver of all assets, undertaking and property of Beta Brands on January 3, 2007. The Receiver subsequently brought a motion for approval of the Bremner Transaction. The order approving the transaction was given on January 5, 2007. In its Reasons, the court described the transaction as "fair and reasonable" producing "a provident sale."

6 There is no issue that, as set out in the Pre-Receivership Report and the Receiver's First Report the Receiver relied exclusively on Capitalink's marketing efforts and reports in recommending that the court direct the Receiver to complete the Bremner Transaction.

7 There is also no issue that, in accordance with the contractual arrangements between Beta Brands and Cap-

italink, Capitalink is entitled to be paid the Capitalink Fee. The issue in contention here is whether the obligation to pay the Capitalink Fee extends to the Receiver.

Positions Advanced on this Motion

8 Mr. Shea, on behalf of Textron, Beta Brands' primary secured creditor, took the position that the Receiver adopted Capitalink's marketing, the court relied on Capitalink's marketing efforts and the Capitalink Fee ought to be paid. He asserted that the principles of unjust enrichment apply to these circumstances -- namely that (1) reliance and enrichment, (2) deprivation and (3) an absence of juristic reason for the enrichment are made out on these facts. He pointed out that the commission fee was always factored into the cash flows presented in connection with the Bremner Transaction, and it was always assumed that the commission would be paid.

9 Mr. Kraft, on behalf of Capitalink, noted that both the Receiver and secured creditor wish to pay the fee, however, his position was that the Receiver was bound by the contract with Capitalink because the Receiver had adopted it by its actions. The quantum meruit claim put forward by Mr. Shea is relied upon as an alternative position. Essentially, Capitalink's position is that the Receiver is bound by the agreement with Capitalink by virtue of the fact that the deal was closed or, alternatively, it is just and equitable for the Capitalink Fee to be paid.

10 Capitalink pointed to the Receivership Order dated January 3, 2007 in support of its position. This Order authorized the Receiver to engage consultants and experts to assist with the exercise of its powers and duties and to market any or all of Beta Brands' property.[FN1] The Receivership Order also included a provision relating to the expenditures or liability incurred by the Receiver in the course of fulfilling its duties:

> **RECEIVER'S ACCOUNTS**
>
> 17. THIS COURT ORDERS that any expenditure or liability which shall properly be made or incurred by the Receiver, including the fees of the Receiver and the fees and disbursements of its legal counsel, incurred at the standard rates and charges of the Receiver and its counsel, shall be allowed to it in passing its accounts and shall form a first charge on the Property in priority to all security interests, trust, liens, charges and encumbrances, statutory or otherwise, in favour of any Person (the "Receiver's Charge").

11 Capitalink submitted that its marketing efforts enabled the Receiver to comply with its obligation to deal with Beta Brands' property in a "commercially reasonable manner." Capitalink states that if its work had not been performed, the Receiver would have had to conduct a marketing process itself or retain someone else to do so to fulfill its statutory obligation under the *BIA*. Any fees incurred by such marketing would have been covered by the Receiver's Charge included in the Receivership Order. Yet, in this case, the Receiver did not incur any fees because of reliance on Capitalink. It is Capitalink's submission that this creates an unjust result.

12 Capitalink also pointed to the Receiver's obligation to act fairly and honestly on behalf of all of the parties that have an interest in the property of Beta Brands. The decisions in *Armadale Properties Ltd. v. 700 King Street (1997) Ltd.* (2001), 25 C.B.R. (4th) 198 (Ont. S.C.J. [Commercial List]) ("*Armadale*") and *Panamericana de Bienes y Servicios S.A. v. Northern Badger Oil & Gas Ltd.* (1991), 8 C.B.R. (3d) 31 (Alta. C.A.) ("*Panamerica*") are submitted in support of this position. According to Capitalink, the Receiver would not be complying with its obligations to act honestly and in good faith if it was entitled to rely on Capitalink's efforts without pay-

ing the Capitalink Fee.

13 The Receiver took the position that it would be dishonourable to resile from Capitalink's claim for the Capitalink Fee, citing *Armadale*, *supra*, and placing considerable emphasis on paragraph 15 which provides as fol- lows:

> The trustee is an officer of the court and must act fairly to all parties with an interest in the estate. It would be dishonourable for the trustee to disclaim this contract. I therefore find that the trustee is bound by the contract in the same manner and to the same extent as the bankrupt was at the time of the bankruptcy and has no power to disclaim the contract.

14 Mr. Grace, on behalf of Local 242, opposed payment of the Capitalink Fee. He did not seek to minimize in any way the work performed by Capitalink but asserted that Capitalink was not entitled to the priority it sought. As Mr. Grace pointed out, there was no authority advanced for the proposition that this unsecured claim of Capitalink should have any priority. In addition, the fact that this payment was reflected in the cash flows presented in the Pre-Receivership Report does not amount to a court endorsement of such payments.

15 Mr. Grace noted that Mr. Shea's position was that the Capitalink Fee should be paid on a quantum meruit basis and he did not advance the position of Mr. Kraft that the Capitalink Fee was a direct obligation of the Receiver. Further, Mr. Grace noted no restitution principles had been cited in any of the materials filed on the mo- tion.

16 In reply, Mr. Shea and Mr. Simpson, on behalf of the Receiver, stated that it was always expected and assumed that the Capitalink Fee would be paid because its work had been relied upon and the fee was fair and reasonable.

17 Mr. Simpson further noted in reply that it always intended to pay the Capitalink Fee and such payment was part of the motion relating to the approval of the Bremner Transaction, however, because of the objections of Local 242, that motion was carved back to the bare minimum, leaving three outstanding issues -- a distribution to Textron (which has since been resolved on consent by an interim distribution order made March 1, 2007), the payment of the Capitalink Fee, and the KERP payments.

18 The issues that must be addressed then, in assessing whether the Receiver is bound by the Capitalink Agreement and therefore required to pay the Capitalink Fee are as follows:

> 1) Has the Receiver, by virtue of its conduct, adopted the arrangements with Capitalink thereby obligating itself to Capitalink? and
>
> 2) Does quantum meruit apply such that the Receiver is required to pay the Capitalink Fee?

(1) Has the Receiver Adopted the Arrangements with Capitalink?

Relevant Legal Principles

19 Section 14.06(1.2) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*") addresses the liability of a trustee or receiver as follows:

Notwithstanding anything in any federal or provincial law, where a Trustee carries on in that position the business of the debtor or continues the employment of the debtor's employees, the trustee is not by reason of that fact personally liable in respect of any claim against the debtor or related to a requirement imposed on the debtor to pay an amount where the claim arose before or upon the trustee's appointment.

20 The section establishes that a receiver is not personally bound or in any way liable under pre-receivership contracts. An exception to this principle arises where there is evidence that the receiver adopted or otherwise agreed to be personally bound by the agreement. See *Howlett v. 512046 B.C. Ltd.* (2000), 17 C.B.R. (4th) 224 (B.C. S.C. [In Chambers]) ("*Howlett*"). As a result, if the claim involved is one for commission on the sale of an insolvent debtor's property, that claim will remain enforceable against the contracting party, but is an unsecured claim in the seller's estate. See *Howlett, supra.*

21 Although the receiver is not generally bound under pre-receivership contracts in accordance with s. 14.06(1.2), the receiver must still comply with certain statutory obligations to act honestly, in good faith and in a commercially reasonable manner. These obligations are set out in s. 247 of the *BIA* as follows:

247. A receiver shall

(a) act honestly and in good faith; and

(b) deal with the property of the insolvent person or the bankrupt in a commercially reasonable manner.

22 Case law has emphasized the obligation of the Receiver to act fairly on behalf of all interested parties. As noted, in *Armadale, supra*, Lax J. described the duty of a Trustee in Bankruptcy at paragraph 15 as a duty to "act fairly to all parties with an interest in the estate." This principle is further emphasized in *Panamericana* at para. 38:

A receiver appointed by the court must act fairly and honestly as a fiduciary on behalf of all parties with an interest in the debtor's property and undertaking. The receiver is not the agent of the debtor or the creditor or of any other party, but has the duty of care, supervision and control which a reasonable person would exercise in the circumstances.

Analysis and Conclusions

23 Although Capitalink is correct in law in setting out the requisite statutory obligations with which the Receiver must comply, such obligations fail to govern the issue involved here, that being priority to payment under the receivership. The Capitalink claim is unsecured and therefore retains no priority to payment within the receivership scheme. As such, Capitalink's claim remains enforceable against Beta Brands, but exists as an unsecured claim in the context of the receivership. The decisions submitted by Capitalink in respect of the Receiver's obligations are distinguishable as they do not involve priority disputes and fail to address the principles limiting the liability of a receiver as set out in section 14.06(1.2) of the *BIA*.

24 In *Armadale, supra*, Deloitte & Touche Inc, in its capacity as Construction Lien Trustee and as Trustee in Bankruptcy brought a motion for direction on whether or not to perform an agreement where the estate would

receive no benefit from the transaction. The court directed the Trustee to complete the transaction. Lax J. pointed to s. 75 of the *BIA*, which prevents a trustee from disclaiming a contract: "An agreement for sale in favour of a bona fide purchaser or mortgagee for valuable consideration is valid and effectual as if no receiving order had been made." See: *Armadale, supra* at para. 11.

25 Lax J. further asserted that even if s. 75 did not apply, the trustee had no right to terminate property rights that had passed under contract prior to the bankruptcy. This determination was based on the equitable interest of the purchaser and the principle of specific performance.

26 These were the primary reasons that the court in *Armadale* ordered the Trustee to proceed with the transaction. The decision did not turn simply on the Trustee's obligations to act fairly to all parties with an interest in the estate. In addition, unlike the circumstances in this case, an agreement of purchase and sale for land was involved in which equitable title had already passed to the purchaser prior to the bankruptcy. This was a significant feature that influenced the court's ultimate determination.

27 It is my view that the principles established in section 14.06(1.2) of the *BIA* govern the result in this motion. The Agreement of Purchase and Sale was executed *before* the Receiver was appointed. The Receiver's reliance on Capitalink's marketing efforts after its appointment was conduct in accordance with its statutory obligation to act in a commercially reasonable manner. There is no evidence which establishes that the Receiver adopted or agreed to be personally bound by the terms of the Agreement.

28 Further, the court order approving the Bremner Transaction did not represent an adoption of, nor did it have the effect of, imposing personal liability on the Receiver for the payment of the commission required pursuant to the Capitalink Agreement. To suggest otherwise would create a result that operates in contrast to the policy interests underlying section 14.06(1.2) designed to insulate receivers from pre-appointment matters that would expose them to liabilities and have the effect of rendering the receivership unviable.

29 In consequence of this conclusion, Capitalink's unsecured claim ranks with all other unsecured claims to which Beta Brands is subject. The Receiver is not bound by the Capitalink Agreement and is not obligated to pay the Capitalink fee.

(2) Quantum Meruit Claim

Relevant Legal Principles

30 As an alternative position, Mr. Shea asserted that the principles of unjust enrichment apply and thereby obligate the Receiver to pay the Capitalink Fee. However, this alternative position was not advanced in the materials filed on this motion and no restitutionary principles were cited in any materials.

31 It is a well-established principle that judges should not decide matters in respect of which the parties have not had an opportunity to make submissions. For example, in *Rodaro v. Royal Bank*, [2002] O.J. No. 1365 (Ont. C.A.) at para. 60, the Court of Appeal stated: "It is fundamental to the litigation process that lawsuits be decided within the boundaries of the pleadings." However, a number of courts have adjudicated on issues of quantum meruit even though they were not specifically pleaded.[FN2] For example, in *Ram Industrial Equipment (Toronto) Ltd. v. Kolson*, [1998] O.J. No. 4531 (Ont. C.A.), at trial, the judge heard submissions on the issue of

quantum meruit even though it had not been included within the pleadings. The trial judge determined that it could properly adjudicate quantum meruit because it had been canvassed throughout the trial and its consideration did not prejudice the defendant. The Court of Appeal affirmed the trial judge's ruling, finding no evidence of prejudice, and ample evidence that the defendant was aware of the quantum meruit issue and had had the opportunity to make submissions on it at trial.

32 In essence, quantum meruit may be adjudicated despite not being sufficiently pleaded in circumstances where there is no prejudice to the opposing party, that party is aware of the issue and was given the opportunity to make submissions on it before the court.

33 Restitutionary quantum meruit is based on principles of unjust enrichment. It may be applied where no contractual relationship exists between the parties, and one party performed services for the other, which benefited that party, on a reasonable expectation that the services were compensable.

34 It is well established that for a claim of unjust enrichment to succeed, there must be:

a. an enrichment;

b. a corresponding deprivation; and,

c. an absence of any juristic reason for the enrichment or non-payment.

35 In *Consulate Ventures Inc. v. Amico Contracting & Engineering (1992) Inc.*, 2007 ONCA 324 (Ont. C.A.), Madam Justice Cronk stated the following in respect of quantum meruit and unjust enrichment at para. 99:

> ...where the claim for restitutionary relief is based on quantum meruit...an explicit mutual agreement to compensate for services rendered is not a prerequisite to recovery. It suffices if the services in question were furnished at the request, or with the encouragement or acquiescence, of the opposing party in circumstances that render it unjust for the opposing party to retain the benefit conferred by the provision of the services.

Analysis and Conclusions

36 Mr. Shea's submissions in respect of quantum meruit should have been included within the materials filed on the motion. He failed to do this or draw the court's attention to any case law in which the principle of quantum meruit was applied successfully against a Receiver. Nonetheless, Mr. Shea and Mr. Grace made submissions on this issue and the quantum meruit argument will be considered in this analysis.

37 In this case, Capitalink and the Receiver did not enter into a contract and, as previously determined, the Receiver was not bound by the agreement. Rather, the contract that was established existed between Capitalink and Beta Brands only. This leaves open the possibility for the application of restitutionary quantum meruit and a consideration of the principles of unjust enrichment.

38 It is my view that the requirements for unjust enrichment and the application of the quantum meruit remedy have not been established in this case.

39 In completing the sale, the Receiver relied on the marketing efforts of Capitalink, thereby avoiding having to undertake any independent marking activities. The Receiver did not have to personally engage additional consultants or experts to assist with the sale or market any of the property through advertising or soliciting offers. The conduct of Capitalink clearly benefited the Receiver thereby satisfying the first essential requirement for an unjust enrichment claim.

40 The second consideration within the unjust enrichment analysis is whether there has been a corresponding deprivation. There is no issue that Capitalink is entitled to be paid the Capitalink Fee in accordance with its contractual arrangements with Beta Brands. The receivership status of Beta Brands means that there is a possibility that Capitalink will be deprived of payment. However, this deprivation does not correspond to the conduct of the Receiver, but rather, to the financial status of Beta Brands. Thus, it appears that the second requirement for the unjust enrichment has not been satisfied.

41 The difficulty that arises in respect of Capitalink's claim is that the efforts rendered by Capitalink did not create a reasonable expectation that such were compensable by the Receiver. Capitalink's arrangement for payment extended only to Beta Brands. Capitalink engaged in marketing efforts in order to fulfill the contractual agreement established with Beta Brands. The court order approving the Bremner Transaction is insufficient to establish a reasonable expectation that the Receiver should compensate Capitalink for its efforts.

42 In addition, this is not a situation where there is an absence of a juristic reason for the enrichment. The Receiver had an obligation to deal with Beta Brands' assets in a commercially reasonable manner. In relying on the marketing efforts of Capitalink, the Receiver was simply complying with this obligation. In my view this represents a sufficient juristic reason for non-payment.

43 Thus, the requirements for the claim of unjust enrichment and quantum meruit have not been satisfied. Although the marketing efforts of Capitalink were relied upon by the Receiver, there was no expectation that Capitalink would receive payment for such efforts and the circumstances of Beta Brands (existing in a state of receivership) do not render it unjust for the Receiver to retain the benefit conferred by the provision of those services in this case.

Part (B): The KERP Payments

Background Facts

44 There had been seven senior management positions in Beta Brands but by the fall of 2006, only three remained -- Mr. Neable, Mr. Musick and Ms. Varallo (the "Key Employees"). Mr. Neable was Vice President, Finance and a director and officer of Beta Brands. Mr. Musick was the President and a director and officer of Beta Brands. Ms. Varallo was the Vice President of Logistics and Beta Brands.

45 As a result of uncertainty concerning the future prospects of Beta Brands, the Key Employees were provided with letters from Beta Brands setting out severance arrangements. The payments included within these letters ranged from $50,000 to $249,000 if the addressee continued in their employment with Beta Brands and the addressee's employment was terminated without cause.

46 As a result of these letters, the Key Employees continued to carry out their duties and responsibilities until

the termination of the employment in January 2007. During their time of employment, the Key Employees performed extensive work in respect of the Bremner Transaction, which included arranging for meetings with members of the Ralcorp team and liaising with Ralcorp executives and engineers to satisfy concerns on the part of those parties with the ability of Beta Brands to achieve an inventory build required by the purchaser.

47 A KERP arrangement was never solidified between the parties. The Key Employees rely on the fact that the secured creditors agreed that the incentive payments totalling $166,000 would be included in the cash flows relating to the Bremner Transaction and would be paid on the closing of the Bremner Transaction. To date, the Receiver has not undertaken to make the KERP Payments, but rather, applies for advice and direction on that point to this court.

Positions Advanced on the Motion

48 The Receiver, Textron and Sun Beta support an order authorizing and directing the Receiver to pay to each of Mr. Neable, Mr. Musick and Ms. Varallo the amount of $66,000. These payments would be made from the realization of the Beta Brands' assets and thus are approved by the secured creditors with the *prima facie* right to receive such proceeds of realization.

49 Mr. Shea, on behalf of Textron, pointed out that a shortfall to Textron and Sun Beta is likely. However, Textron and Sun Beta do not object to the KERP Payments being made from the proceeds of realization of the Beta Brands' assets because they consider the management team a key part of the conclusion of the Bremner Transaction. The management team was essential to the inventory build, a key aspect of the arrangements with Bremner. Mr. Shea asserted that these payments were, in essence, a reward when the deal closed for getting the job done and he asserts that it was appropriate business judgment that Beta Brands enter into these arrange- ments.

50 Mr. Weisz confirmed Sun Beta's position that there was no contract between Textron or Sun Beta and the key three employees and thus no liability to those individuals. However, both secured creditors were consulted regarding these arrangements and did not object to the KERP payments being made out of the cash flow from the closing of the Bremner Transaction.

51 Mr. Simpson, on behalf of the Receiver, took the position that the Receiver should not disclaim these arrangements and, as a matter of commercial reasonableness and morality where the Receiver relies on third parties and consultants, they should be paid. As he indicated, it may be that such payments would have the effect of "jumping the queue" but the Receiver did not view that as a compelling factor to not authorize the payments considering the Receiver's use of the efforts of the employees. He referred, again, to *Armadale, supra.*

52 Mr. Highley, on behalf of the employees, asserted that the KERP Payments are not a severance payment in any way and he noted that if the plant had shut down in October and the employees had not succumbed to inducements, the Bremner Transaction could not have been negotiated and there would have been no way to complete the inventory build and more than likely the Receiver would have been appointed much earlier at significant expense. He asserted that the contributions of the three senior managers reduced realization costs; they assumed extraordinary duties and extensive workload; and their efforts generated a large amount of money. His position was that their claimed fee is fair and reasonable, particularly given that these three employees not only ran the plant, but created the conditions for the sale to Bremner and indeed "shepherded" the deal from the ori-

ginal negotiations to conclusion.

53 Mr. Highley asserted that the payment to these Key Employees could be justified on the basis of: (a) inducement; (b) realization; (c) costs of realization; and (d) work load. However, Mr. Highley was unable to draw the court's attention to any case law that supported his argument seeking the KERP payments.

54 Mr. Grace, on behalf of Local 242, emphasized that the issue is whether the Receiver has the authority to make the KERP Payment out of the realization proceeds in these circumstances, where such payment will in all probability increase the deficiency to Textron and Sun Media and thus increase the probability that there will be no proceeds available to the unsecured creditors, including but not limited to the employees of Beta Brands.

Relevant Legal Principles

55 KERP arrangements, also referred to as "pay to stay" compensation plans, are typically the subject of careful review before being paid out. This principle applies even in the context of a restructuring process designed to preserve the debtor and its business:

> KERPs and special director compensation arrangements are heavily negotiated and controversial arrangements...Because of the controversial nature of KERP arrangements, it is important that any proposed KERP be scrutinized carefully by the monitor with a view to insisting that only true key employees are covered by the plan and that the KERP will not do more harm than good by failing to include the truly key employees and failing to treat them fairly.
>
> Because any KERP arrangement is intended to secure key personnel for the duration of the restructuring process, the additional compensation offered to the affected employees should be deferred until after the restructuring or sale of the business or assets has been completed. In many cases, employees will require staged "stay bonuses" that are payable at specified times in the future if they stay until that time.
>
> *Warehouse Drug Store Ltd., Re*, [2006] O.J. No. 3416 (Ont. S.C.J.) at para. 14 ("*Warehouse Drug Store*") referring to Kevin McElcheran, *Canadian Insolvency in Canada* (LexisNexis-Butterworths) at 231.

56 The court in *Warehouse Drug Store, supra*, accepted these principles, but determined that the circumstances involved in that case could be distinguished based on the facts. In that case, the court dealt with a motion to determine whether the former CFO of Warehouse Drug Store Ltd., ("Warehouse"), should be entitled to recover a "retention bonus" established within the terms of a termination agreement. The CFO was persuaded by this agreement to forego alternative employment he had acquired and remain employed with Warehouse during its restructuring process which subsequently turned into a realization process.

57 After Warehouse filed under the *Companies' Creditors Arrangement Act*, the termination agreement was made known to the Monitor but was not noted in any Monitor's report until after the transaction that triggered the CFOs termination was in process. Despite this error, Campbell J. ordered the payment of the retention bonus, asserting at paragraph 9 that it was "reasonable to infer that had the issue of the termination agreement been included in a report to the Court soon after the appointment of the Monitor, it would likely have been approved."

58 Mr. Grace referred to the principles established by American case law in respect of KERP payments and specifically the decision in *Global Home Products, LLC, Re* [369 B.R. 778 (U.S. Bankr. D. Del. 2007)] Case No. 06- 10340, which established the requirements that must be satisfied before the court can approve a "pay for value" compensation or incentive plan:

a. there is a reasonable relationship between the plan proposed and the results to be obtained;

b. the cost of the plan is reasonable in the context of the debtor's assets, liabilities and earning po- tential;

c. the scope of the plan is fair and reasonable in that it either applies to all employees or treats them differently for rational and fair reasons;

d. the plan is consistent with industry standards;

e. the debtor has undertaken a reasonable investigation to determine the need for an incentive plan, has analyzed which key employees need to be incentivised and what is generally applicable in a particular industry; and

f. the debtor received independent counsel in performing the diligence and in creating and authorizing the incentive compensation or, alternatively, there were good and valid reasons why such independent counsel was not utilized or needed.

59 It is noteworthy to point out that the payment of KERPs in the United States is governed by restrictive legislation that require insolvent debtors to satisfy rigorous standards before the court can approve the payment of KERPs or severance payments to insiders of an insolvent company. Equivalent legislative principles have not been established in Canada. In addition, the principles established in *Global Home Products, supra*, have not been adopted by Canadian case law.

Analysis and Conclusions

60 It is apparent that the circumstances involved in *Warehouse Drug Store, supra*, are distinct from those involved in this case. Unlike the CFO in that decision, there has been no suggestion that any of the Key Employees had alternative employment opportunities that they chose to forego upon receipt of the letters setting out the severance arrangement or when the Bremner Transaction was in play. Further, Beta Brands did not reorganize during the relevant period of time. The efforts of these three employees were designed, seemingly, to ensure that the Bremner Transaction could be completed on terms acceptable to Textron.

61 Despite these distinctions, the principles enunciated by the court in respect of the KERP payments remain applicable and relevant to these proceedings. The proposed KERP payments in this case must be subject to careful scrutiny.

62 In this case, the court is being asked to approve KERP payments for which there is no contractual basis. Such payments have not been reviewed by the Receiver, nor has the Receiver submitted any comment in respect of these payments in any report. In addition, the extent to which the services rendered by these employees went beyond their normal duties as salaried members of senior management is unclear.

63 As a result, there is a very thin evidentiary record before the court. I agree with Mr. Grace that these former employees, who worked to get the Bremner Transaction completed and to build the inventory are attempting to "jump the queue" of unsecured creditors in advancing this claim.

64 In addition, the circumstances indicate that the payments sought by these employees are more in the nature of a severance payment than a KERP payment. As noted, a KERP agreement was never concluded between the parties. The payments were arranged at a time when Beta Brands had written severance arrangements in place. Thus, the payments are in substance payments in lieu of severance and were designed to replace those severance arrangements.

65 Even if the payment in issue is properly characterized as a KERP, it is not entitled to statutory priority or preference. In essence, those who support the payment being made now rely on the fact that the payment was reflected in the cash flow projections that were acceptable to the largest secured creditors.

66 For these reasons, it seems to me that it is inappropriate to order the Receiver to make the payments requested by Mr. Neable, Mr. Musick and Ms. Varallo. There is no legal basis for them to acquire priority over other creditors including other employees seeking termination and severance pay.

Summary of Conclusions

67 Capitalink's request for an order authorizing and obligating the Receiver to pay the Capitalink Fee is denied. The Receiver is not bound by the Capitalink Agreement and therefore not obligated to pay the Capitalink Fee. Capitalink's unsecured claim ranks with all other unsecured claims to which Beta Brands is subject.

68 The Receiver is not obligated to make the payments in the amount of $66,000 each being claimed by Mr. Neable, Mr. Musick and Ms. Varallo (the KERP Payments).

Order accordingly.

FN1. These powers are found specifically within paragraphs 3(d) and 3(k) of the Receivership Order

FN2. See: *Hoffer v. Verdone*, [1994] O.J. No. 1967 (Ont. Gen. Div.); *Honey-Bee Sanitation Inc. v. Essex (County)*, [1993] O.J. No. 178 (Ont. Gen. Div.); *Hill v. Develcon Electronics Ltd.*, [1991] S.J. No. 311 (Sask. Q.B.); *Johnson v. H.G. Precision Machine Ltd.*, [1991] B.C.J. No. 843 (B.C. S.C.); *Aurora Development Ltd. v. Paradise (Town)* (1991), 90 Nfld. & P.E.I.R. 5 (Nfld. T.D.).

END OF DOCUMENT

TAB 7

2006 CarswellOnt 5128

Warehouse Drug Store Ltd., Re
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 THE WAREHOUSE DRUG STORE LTD. AND THE COMPANIES LISTED IN SCHEDULE "A" HERETO
APPLICATION UNDER THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS AMENDED
Ontario Superior Court of Justice
C. Campbell J.
Heard: August 15, 2006
Judgment: August 22, 2006
Docket: 05-CL-5880

Counsel: Raymond Slattery for McKesson Canada Corporation

Clifford Cole for Moving Party, Larry Cooper

Subject: Insolvency; Labour and Employment; Public

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

Retention bonus -- W Ltd. filed under Companies' Creditors Arrangement Act with support of secured creditor in April -- At time of initial and restated order in June, employee was chief financial officer of W Ltd. and related companies with salary of $140,000 -- Employee had obtained alternative employment in May but was persuaded by principals of W Ltd. to stay -- Agreement provided for payment of termination amount which was lodged with W Ltd.'s solicitors -- Letter agreement was made subject to approval of senior secured creditor -- No notice to secured creditor was given nor approval sought -- Employee brought motion for determination of whether he should be entitled to recover sum of $100,000 -- Secured creditor objected -- Motion granted -- It was reasonable to infer that had issue of termination agreement been included in report to Court soon after appointment of Monitor, it would likely have been approved -- Senior unsecured creditor did approve of payment -- What was defined as "Termination amount" was payable only if employee remained employed and Restructuring Process turned into Realization Process, which is what occurred -- Termination agreement was intended to and did meet requirements for "retention bonus" as provided for in initial order -- There was no suggestion whatever that fact of agreement was purposely being kept secret or that employee had anything to do with information being withheld -- Termination agreement was entered into on bona fide basis within terms of initial order, which provided for it and should now be upheld -- Order sought by employee was allowed and his entitlement to money held by solicitors confirmed.

MOTION by employee for determination of whether he should be entitled to recover sum of $100,000.

C. Campbell J.:

1 This is a motion to determine whether the former CFO of Warehouse Drug Store Ltd. ("Warehouse") should be entitled to recover the sum of $100,000 in respect of what has variously been called a "retention bonus" and a "termination amount."

2 The initial filing of Warehouse under the *Companies' Creditors Arrangement Act* ("CCAA") was made in April 2005 with the support of McKesson, the objecting secured creditor on this motion.

3 At the time of the Initial and Restated Order in June 2005, Mr. Larry Cooper was the Chief Financial Officer of Warehouse and related companies, with a salary of $140,000 and an employment agreement entitling him to six months' severance in the event of termination.

4 As a result of the initial filing, Cooper was concerned about his future and sought and obtained alternative employment in May 2005.

5 Cooper was persuaded by the principals of Warehouse to stay, as his continued employment was regarded as essential to what was then hoped to be a successful restructuring of the Company.

6 The operative portions of the agreement reached between the Company and Mr. Cooper are set out below:

> 1. Subject to paragraph 3 of this letter agreement, in the event that:
>
> > (i) a plan of compromise and arrangement (the "Restructuring Plan") pursuant to the *Companies' Creditors Arrangement Act* (the "CCAA") or *Bankruptcy and Insolvency Act* (the "BIA") is not approved or the sanction by the Court of the Restructuring Plan is not obtained and, as a result, the business and assets of H&Z are to be liquidated (the "Realization Process"); and
> >
> > (ii) you agree in writing to remain employed by H&Z or any Trustee in Bankruptcy of H&Z or by any Receiver of the assets and property of H&Z for not less than 90 days in order to assist in the Realization Process,
>
> you will be entitled to the Termination Amount provided you remain employed throughout such 90 day period.
>
> .....
>
> 3. The payment of the Termination Amount will fully satisfy your entitlement under applicable law and any agreement between you and any H&Z entity in respect of the termination of your employment including, without limitation, your entitlement under the *Employment Standards Act* (Ontario) and at common law.

7 The Termination Amount was, pursuant to further terms, lodged with the solicitors of the Company. The let-

ter agreement was also made subject to the approval of the senior secured creditor, since further financing from it was being provided. No notice to McKesson was given nor approval from McKesson sought.

8 The agreement was made known to the Monitor but unfortunately was not noted in any Monitor's report until after the transaction that triggered Mr. Cooper's termination was in process.

9 On the material before me, I can conclude that it is reasonable to infer that had the issue of the termination agreement been included in a report to the Court soon after the appointment of the Monitor, it would likely have been approved.

10 At the time of the execution of the Termination Agreement, the future of Warehouse was largely unknown. The senior unsecured creditor did and does approve of the payment.

11 The major objection raised by McKesson is that the payment now sought to be made to Cooper does not come within the phrase "retention bonus," which was authorized in the Initial CCAA Order.

12 Mr. Slattery submits that the purpose of a retention bonus is to encourage key employees to stay with the Company to accomplish a successful restructuring and earn the bonus, which is to be distinguished from the agreement in question, which in his view should be regarded as a severance agreement.

13 In addition, it is submitted that since the concept of a "retention bonus" is unknown to Canadian insolvency law, it should be construed narrowly in the context of a CCAA Order.

14 The only authority relied on in support of the above propositions is from *Canadian Insolvency in Canada* by Kevin P. McElcheran (LexisNexis -- Butterworths) at p. 231, under the heading "Director and Officer Compensation -- Key Employee Retention Plans:

> KERPs and special director compensation arrangements are heavily negotiated and controversial arrangements. In insolvency cases, there is plenty of blame to go around for the debtor company's financial failure. The first target for that blame is the existing management group. Accepting that the existing management group should receive additional compensation (beyond their existing perhaps bloated compensation packages) to fix their own mistakes (a common creditor and employee perception) is difficult for many stakeholders. ... Sometimes a KERP is necessary to encourage them to stay the course of the restructuring. Because of the controversial nature of KERP arrangements, it is important that any proposed KERP be scrutinized carefully by the monitor with a view to insisting that only true key employees are covered by the plan and that the KERP will not do more harm than good by failing to include the truly key employees and failing to treat them fairly.
>
> Because any KERP arrangement is intended to secure key personnel for the duration of the restructuring process, the additional compensation offered to the affected employees should be deferred until after the restructuring or sale of the business or assets has been completed. In many cases, employees will require staged "stay bonuses" that are payable at specified times in the future if they stay until that time.

15 I accept the generality of the above comments but am of the view that the circumstances here can be distinguished from the facts before me.

16 In my view, what is defined as the Termination Amount is payable only if Cooper remains employed and the Restructuring Process turns into a Realization Process, which is what occurred. Mr. Cooper is the only member of management to receive the benefit of such an agreement.

17 It was also suggested that the condition in paragraph 1(ii) was not met because Mr. Cooper quit less than 90 days after the failure of the Restructuring Plan. Mr. Cooper's employment was terminated as a result of the Order of this Court transferring assets. Mr. Cooper did provide the assistance the paragraph anticipated.

18 I am satisfied that the Termination Agreement was intended to and does meet the requirements of a "retention bonus" as provided for in the Initial Order.

19 I can understand and have sympathy for the annoyance created in McKesson only learning well after the fact about the Termination Agreement. There is no suggestion whatever that the fact of the Agreement was purposely kept a secret or that Mr. Cooper had anything to do with the information being withheld.

20 One of the major concerns of McKesson is that the effect of the asset sale transaction is such that Mr. Cooper will obtain employment with a new entity owned by the same people as previously owned Warehouse, doing the same job with potentially the same financial terms as previously.

21 If the Termination Agreement had been executed much closer to the date of the asset sale, or if in June 2005 either the first secured creditor opposed to the agreement, there might be a different result.

22 In the circumstances, I am satisfied that the Termination Agreement was entered into on a bona fide basis within the terms of the Initial Order, which provided for it and should now be upheld.

23 As a result, the Order sought by the moving party Cooper is allowed and his entitlement to the monies held by the solicitors is confirmed.

24 If it is necessary to deal with the issue of costs, counsel should forward submissions in writing within the next two weeks.

Motion granted.

END OF DOCUMENT

Court File No: CV-09-8247-00CL

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 SALES INC. and GRANT U.S. HOLDINGS GP (the "Applicants")

ONTARIO

SUPERIOR COURT OF JUSTICE

PROCEEDING COMMENCED AT TORONTO

BRIEF OF AUTHORITIES
(Motion returnable August 6, 2009)

FRASER MILNER CASGRAIN LLP
1 First Canadian Place
100 King Street West,
Toronto, Ontario
M5X 1B2

Lawyer: Daniel R. Dowdall / Jane Dietrich
LSUC: 16737D / 49302U
Email: dan.dowdall@fmc-law.com
jane.dietrich@fmc-law.com
Telephone: 416 863-4700 / 416-863-4467
Facsimile: 416 863-4592

Lawyers for the Applicants Grant Forest Products Inc., Grant Alberta Inc., Grant Forest Products Sales Inc., and Grant U.S. Holdings GP

7111394_1.DOC