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")

FACTUM
(Motion returnable August 6, 2009)

August 4, 2009

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Overview

1. The Applicants file this factum in opposition to a motion by GE Canada Leasing Services Company ("**GE Canada**") whereby GE Canada is seeking to amend the order of Justice Newbould made on June 5, 2009 (the "**Initial Order**") which granted the Applicants protection under the *Companies' Creditors Arrangement Act* (the "**CCAA**").

2. The Applicants oppose GE Canada's motion to remove the provisions (the "**KERP Provisions**") in the Initial Order which:

   (a) approve a key employee retention plan agreement dated December 19, 2009 between Peter Lynch and Grant Forest Products Inc. ("**Grant Forest**") as amended by an amendment agreement dated as of April 1, 2009 (collectively, the "**KERP Agreement**") which provides for a payment to him of 3 times his base salary; and

(b) create a charge over the property of the Applicants in the maximum amount of $1,134,000 (the "**KERP Charge**") as security for all amounts owing to Peter Lynch pursuant to the KERP Agreement.

3. The Applicants and key stakeholders, including The Toronto-Dominion Bank as agent (the "**Agent**") for the first lien lenders (the "**First Lien Lenders**"), the board of directors of Grant Forest Products Inc. (the "**Board**") which includes 4 experienced independent board members, the chief restructuring advisor, Stonecrest Capital Inc. (the "**CRA**"), and Ernst &Young Inc. in its capacity as court appointed Monitor of the Applicants (the "**Monitor**") support the continuation of the KERP Provisions. In making the decision to support the KERP Provisions these parties have determined, in exercising their business judgement, that the KERP Provisions create value for the stakeholders in that they act to ensure that Peter Lynch will continue to provide the Applicants with his unique skills, knowledge and expertise during the Applicants' CCAA proceedings.

4. GE Canada has put forward no evidence which contradicts the evidence submitted by the Applicants and the Monitor that Peter Lynch is critical to the Applicants and their stakeholders or that the value of the KERP Provisions outweighs the cost associated with them.

5. It is far from certain that those stakeholders who have priority over unsecured creditors (including the First Lien Lenders who are owed approximately $400 million USD and the Second Lien Lenders who are owed approximately $150 million USD in principal plus accrued interest of approximately $50 million USD) will recover payment in full of amounts owing to them by the Applicants. In a situation where those parties either support (or, in the case of the Second Lien Lenders, have not objected to) the KERP Provisions, the Court should not remove the KERP Provisions, based on the objection of one, of many, unsecured creditors.

Facts

A. Peter Lynch provides unique and irreplaceable value

6. Peter Lynch is the executive vice president and secretary of Grant Forest, the vice president and secretary of Grant Alberta Inc. ("**Alberta**") and the president and secretary of Grant Forest Products Sales Inc. ("**Sales**"). He is also director of each of Grant Forest, Alberta and Sales.

> Affidavit of Hap Stephen sworn July 22, 2009 (the "Stephen Affidavit") at para 13.

7. Peter Lynch has been employed as a senior officer of Grant Forest and other related subsidiaries since 1993, has been involved in the Grant Forest business since the early 1980s first as external legal counsel and subsequently as an officer. He is the only experienced senior officer of the Applicants who is not a member of the Grant family and does not have any equity interest in the Applicants or any related entities.

> Stephen Affidavit at para 15.
>
> Transcript of Peter Lynch at question 13.

8. The Monitor and key stakeholders, including the Board, the CRA and the Agent for the First Lien Lenders, support the KERP Provisions contained in the Initial Order as they recognize the critical value of Lynch to the stakeholders during the CCAA process.

> Stephen Affidavit at para 20-23.
>
> Third Report of Ernst & Young Inc. as court appointed Monitor dated July 31, 2009 (the "**Third Report**") at para 24.

9. GE Canada, which claims that it is an unsecured creditor of Grant Forest for a deficiency claim of approximately $6 million, is the only person opposing the KERP Provisions.

> Affidavit of Ryan Stills sworn July 9th, 2009 at para 1.

10. None of the many other arms length and non arms length unsecured creditors, including 1308406 Ontario Inc., who is owed approximately $50 million, Grant Forest Products Corp. who is owed approximately $6.1 million and Peter Grant Sr. who has a contingent unsecured claim of approximately $10 million has objected to the KERP Provisions.

Affidavit of Peter Lynch sworn June 24, 2009 at para 40.

B. Peter Lynch is essential to the management and operations of the Applicants

11. Peter Lynch has extensive knowledge of all aspects of the operations and history of the Applicants' businesses and their financings and is critical in dealing not only with potential investors during this key point in the CCAA proceedings but also in making daily decisions regarding the operations and management of the Applicants' businesses.

Stephen Affidavit at para 14, 15 and 18.

12. There is no other individual with the experience, expertise and knowledge of Peter Lynch within the Applicants' organization to perform his current duties. As well, there is no duplication in the roles of the CRA and Peter Lynch.

Stephen Affidavit at para 16 and 24.

13. Peter Lynch was also a key point person for Grant Forest in respect of the marketing process that was initiated prior to the commencement of the CCAA process and his knowledge in this regard assists in ensuring that the current Marketting Process is conducted in an efficient and effective manner.

The Third Report at para 14.

14. Further, it would be extremely difficult to find a replacement for Peter Lynch either within or outside the Applicants. If Peter Lynch were to leave, the delay, uncertainty and expense of finding a replacement for him (who will most likely have inferior knowledge) would far outweigh any benefit that may be received by the stakeholders in failing to make the payments when due as set out in the KERP Agreement.

Stephen Affidavit at para 24.

15. The KERP Agreement payment is for an amount equal to three times Peter Lynch's base salary (properly, $1,134,000). The amendment to the KERP Agreement made as of April 1, 2009 mistakenly calculates such amount to be $1,050,000.

Transcript of Peter Lynch at question 378.

16. Peter Lynch received an unsolicited overture for a CEO position at approximately the time the Applicants made their CCAA filing, and the KERP Provisions were a factor in his decision not to pursue the overture.

> Transcript of Peter Lynch at questions 266-271 and 463.

Issues and the Law

17. The issue to be determined on this motion is whether the Court should preserve the KERP Provisions in the Initial Order.

18. Courts have authorized key employee retention plans where 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*".

> *Houlden & Morawetz Bankruptcy and Insolvency Analysis, Companies' Creditors Arrangement Act*, Sections 11-11.11, N§79 – Key Employee Retention Plans and Key Employee Incentive Plans.

19. In approving key employment retention plans, the Court has held that a key employee retention plan should be closely scrutinized by the Court but, in Canadian insolvency proceedings, unlike under the U.S. Bankruptcy Code, there is no formal list of requirements which must be met in order for the Court to approve a key employee retention plan.

> *Warehouse Drug Store Ltd., Re.* (2006) 24 C.B.R. (5th) 275, 2006 CarswellOnt 5128 (Ont. Sup. Ct. Commercial List) at para 15 and 22.

> *Textron Financial Canada Ltd. v. Beta Ltee/Beta Brands Ltd.* (2007) 36 C.B.R. (5th) 296, 2007 CarswellOnt 5799 (Ont. Sup. Ct.) at para 59.

The KERP is specifically addressed toward maintaining Peter Lynch's skills and knowledge

20. It is an accepted purpose of a key employee retention program to retain employees with critical skills within the insolvent company at a time when they are likely to look for other employment because of the company's financial distress.

> *Nortel Networks Corp., Re.*, 2009 CarswellOnt 1330 (Ont. Sup. Ct. Commercial List) at para. 4.
>
> *Nortel Networks Corp., Re.*, 2009 CarswellOnt 1519 (Ont. Sup. Ct. Commercial List).

21. To date, the KERP Provisions have created an incentive for Peter Lynch to not pursue an unsolicited overture of employment as a CEO which he received at about the commencement of the CCAA proceedings. Should the KERP Provisions be removed, the incentive for Peter Lynch to remain with the Applicants during their restructuring will be lost and Peter Lynch will be more likely to pursue alternate employment opportunities.

> Transcript of Peter Lynch at question 463.

22. GE Canada, in its factum, relies on two decisions where charges for key employment retention plans have not been approved by the Court. Both can be clearly distinguished from the present circumstances:

    (a) In *Textron Financial Canada Ltd. v. Beta Ltee/Beta Brands Ltd.*, the issue considered by the Court was whether payments due under a key employee retention agreement (which had not been executed) but which appear to have been agreed to by a Debtor and fully performed prior to the appointment of the receiver should be honoured by the receiver. Here the agreement has been adopted as a post filing obligation well prior to complete performance or the amount payable having been earned; and

    > *Textron Financial Canada Ltd. v. Beta Ltee/Beta Brands Ltd. supra* at para 47.

    (b) In *MEI Computer Technology Group Inc., Re,* the employee retention charge, which the Court was being asked to approve, was requested to rank subordinate to existing secured creditors. The Court found it difficult to understand why the charge, if it was essential to a restructuring, was only created at the expense of the unsecured creditors and not the secured creditors. Unlike this situation, in *MEI Computer Technology*, the retention plan did not represent a considered business judgement of stakeholders as there, the unsecured creditors were essentially unrepresented and the secured creditor had no reason to be concerned since the charge was subordinate to its interest. In the case currently before this Court, the KERP Charge ranks ahead of the First Lien Holder's security, who support the KERP Provisions in a situation where it is uncertain that they will be paid in full and represents that key stakeholder's view that this cost is appropriate.

MEI Computer Technology Group Inc., Re 2005 CarswellQue 3675 (Que. Sup. Ct.) at para 26.

Summary

23. The Monitor supports the KERP Provisions and key stakeholders, including the Agent for the First Lien Lenders, the Board (relying upon independent counsel) and the CRA have, in exercising their business judgement, determined that the value to the Applicants and their stakeholders of retaining Peter Lynch outweighs the cost of the KERP Provisions.

Stephen Affidavit at para 21-23.

The Third Report at para 24.

24. In this respect, the support by the Agent for the First Lien Lenders, who have relied on their financial advisor, PricewaterhouseCoopers, is telling as there is no assurance that the First Lien Lenders will see a full recovery and thus the First Lien Lenders may very well shoulder the full cost of the KERP Provisions.

Transcript of Hap Stephen at questions 113-115.

25. As well, the Court has held that, the Court should be reluctant to second guess considered business decisions of a Court Officer. There are no circumstances here which would justify interfering with the Monitor's recommendation in support of the KERP Provisions for Peter Lynch.

Royal Bank v. Soundair Corp. 1991 CarswellOnt (Ont. C.A.) at para 14.

Tiger Brand Knitting Co., Re 2005 CarswellOnt. 1240 (Ont. Sup. Ct. Commercial List) at para 35.

26. GE Canada is only one of many unsecured creditors of the Applicants. GE Canada has put forward no evidence to contradict the evidence of the Monitor and the Applicants that the KERP Provisions are appropriate in the circumstances. GE Canada is the only person that is objecting to the KERP Provisions. In these circumstances, the Court should not accede to GE Canada's objection .

Order Requested

27. The Applicants hereby request that the Court dismiss the motion of GE Canada in its entirety and award costs of this motion against GE Canada.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 4th day of August, 2009.

Daniel R. Dowdall
FRASER MILNER CASGRAIN LLP

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

Schedule "A"
List of Authorities

1. *Holden & Morawetz Bankruptcy and Insolvency Analysis, Companies' Creditors Arrangement Act*, Sections 11-11.11, N§79 – Key Employee Retention Plans and Key Employee Incentive Plans.

2. *MEI Computer Technology Group Inc., Re.*, [2005] R.J.Q. 1558, 2005 CarswellQue 3675 (Que. Sup. Ct.).

3. *Nortel Networks Corp., Re.*, 2009 CarswellOnt 1330 (Ont. Sup. Ct. Commercial List); and *Nortel Networks Corp., Re.*, 2009 CarswellOnt1519 (Ont. Sup. Ct. Commercial List).

4. *Royal Bank v. Soundair Corp.* (1991), 7 C.B.R. (3d) 1, 1991 CarswellOnt 205 (O.C.A.).

5. *Textron Financial Canada Ltd. v. Beta Ltee/Beta Brands Ltd.* (2007), 36 C.B.R. (5^{th}) 296, 2007 CarswellOnt 5799 (Ont. Sup. Ct.).

6. *Tiger Brand Knitting Co., Re.* (2005), 9 C.B.R.(5^{th}) 315, 2005 CarswellOnt 1240 (Ont. Sup. Ct.).

7. *Warehouse Drug Store Ltd., Re.* (2006), 24 C.B.R. (5^{th}) 275, 2006 CarswellOnt 5128 (Ont. Sup. Ct. Commercial List).

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