Court of Appeal File No. M52471
Superior Court File No.: CV-21-656040-00CL

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 LAURENTIAN UNIVERSITY OF SUDBURY

BOOK OF AUTHORITIES OF THE MOVING PARTY

(Motion by Thorneloe University for Leave to Appeal)

May 25, 2021

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Nova Scotia Supreme Court

Laserworks Computer Services Inc., Re

1997 CarswellNS 179, [1997] N.S.J. No. 564, 46 C.B.R. (3d) 226

In the Matter of the Proposal of Laserworks Computer Services Inc.

Registrar Hill

Judgment: April 14, 1997
Docket: 19853

Proceedings: affirmed (August 13, 1997), Doc. No. B19853/97 (N.S.S.C.)

Counsel: *Roy F. Redgrave* and *Cynthia Isenor*, for Laserworks Computer Services Inc.
A. James Musgrave, for 3004876 Nova Scotia Limited.
D. Bruce Clarke, for Trustee McCuaig & Company Inc.

Table of Authorities

Cases considered by *Registrar Hill*:

De La Hooke, Re (1934), 15 C.B.R. 485 (Ont. S.C.) — applied

Dimples Diapers Inc. v. Paperboard Industries Corp. (1992), 15 C.B.R. (3d) 204 (Ont. Gen. Div.) — applied

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Loxtave Buildings of Canada Ltd., Re (1943), 25 C.B.R. 22 (Sask. K.B.) — considered

McKewan v. Sanderson (1873), L.R. 15 Eq. 229 (Eng. V.-C.) — referred to

Newlands Textiles Inc. v. Carrier (1983), 47 C.B.R. (N.S.) 148 (Ont. S.C.) — referred to

Pappy's Good Eats Ltd., Re (1985), 56 C.B.R. (N.S.) 304 (Ont. S.C.) — applied

Sadler Manufacturing Co. v. Golt (1954), 35 C.B.R. 67, [1955] Que. S.C. 69 (C.S. Que.) — referred to

Shepard, Re (1996), 40 C.B.R. (3d) 145, (sub nom. *Shepard (Receivership), Re)* 109 Man. R. (2d) 306 (Man. Master) — applied

Teac Canada Ltd. c. Bédard Louis Inc. (1991), 52 Q.A.C. 108, (sub nom. *Bédard Louis Inc., Re)* 22 C.B.R. (3d) 218, (sub nom. *Bédard Louis Inc. c. Teac Canada Ltd.)* [1992] R.L. 640 (C.A. Que.) — distinguished

Statutes considered:

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

Generally — considered

Pt. III — referred to

s. 2 "court" — considered

s. 50 — referred to

s. 57(a) — considered

s. 108(3) — referred to

s. 163(2) — referred to

s. 183(1) — considered

s. 192(1)(h) — considered

***Registar Hill*:**

1 This application came on for hearing on Friday last. At the close of the hearing I indicated to counsel that I would reflect over the weekend and give a decision today, as the proposal is currently in limbo awaiting the result.

2 The application raises an issue with the potential to have some real impact on commercial entities seeking to make proposals under Part III of the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, as amended (the "B.I.A."). It calls into question the efficacy of the proposal process. The circumstances demand an immediate response from this Court, both to resolve this controversy and to give guidance to parties that might be inclined to similar activity in the future. I begin with a short review of the facts.

The Facts

3 On December 4, 1996, Laserworks Computer Services Inc. ("Laserworks") gave notice of its intention to file a proposal under the provisions of section 50 of the B.I.A. The proposal was filed on January 3, 1997. The first meeting of creditors convened on January 24, 1997, and was adjourned. On February 12, 1997, Laserworks filed an amended proposal. The meeting of creditors was reconvened on March 3, 1997, to consider the amended proposal.

4 Mr. Victor Goldberg, a solicitor, attended at the meeting and presented eighteen proxies whereby creditors had given their proxy to either Mr. Goldberg or Mr. James Enman, an associate of Mr. Goldberg. The principals of Laserworks took objection to the eighteen claims represented by Mr. Goldberg's proxies. It was alleged that Mr. Goldberg was acting on behalf of a competitor purchasing claims and soliciting proxies.

5 The chairperson of the meeting put certain questions to Mr. Goldberg. The minutes of the meeting are in evidence before me, and it is interesting to refer to those minutes which if nothing else give some appreciation of the flavour of the meeting:

> The chairperson asked Mr. Goldberg if he had paid any creditors for their proxies. Mr. Goldberg replied that there was nothing wrong with this practice. The chairperson again posed the same question to Mr. Goldberg. Mr. Goldberg replied that this practice was acceptable if there has been an agreement to assign claims. The chairperson was not aware of any assignment of claims. Mr. Goldberg advised that there may have been assignments. The chairperson advised Mr. Goldberg that there were no assignments of claims of which she was aware. Mr. Goldberg pointed out that he had never said there were not any assignments of claims. The chairperson asked Mr. Goldberg if he had made payments for any proxies. Mr. Goldberg replied that he had not. The chairperson advised that an assignment of claims may very well affect the number of claims able to vote, and asked Mr. Goldberg if any claims had been assigned. Mr. Goldberg responded that it may be that claims had been assigned, but none had been accepted.
>
> Bruce Clarke, counsel for the trustee, asked Mr. Goldberg if any money had been paid to the creditors. Mr. Goldberg replied that payment had been made "only on some". Mr. Clarke asked Mr. Goldberg if the numbered company referred to in the assignment document was obligated to make payment to certain of the creditors. Mr. Goldberg asked Mr. Clarke what difference this would make. The chairperson replied that this may be a significant issue as it may be indicative of an execution of an assignment of claims.

6 It is not unfair to say that Mr. Goldberg was obtuse to a very great degree. While this does not necessarily confirm suspicion as to the motives of his client, it does explain the concern expressed by the principals of Laserworks.

7 Mr. Goldberg objected to the claims of four creditors. As I have noted, the claims of the eighteen creditors represented by Mr. Goldberg's proxies were also objected to. The chairperson of the meeting proceeded pursuant to section 108(3) of the B.I.A. and marked the claims objected to, but allowed the creditors to vote subject to their votes being declared invalid in the event this court should sustain the objections.

8 Upon the vote being taken, fourteen creditors with a total claim value of $206,531.65 voted in favour of the proposal. Twenty creditors with a total claim of $140,370.00 voted against the proposal. Thus 41% of creditors representing 59.5% of the claims voted pro, and 59% of the creditors with 40.5% of the claims voted con. The proposal was defeated, subject to the resolution of the objections before the court today.

9 It is common ground that should the objection against the votes of those eighteen creditors for whom Mr. Goldberg held the proxy be sustained, the proposal would be approved. This would be the case even if the objection of Mr. Goldberg to the four additional creditors' claims were sustained.

10 The meeting of creditors now stands adjourned pending the disposition of this application.

11 Prior to the hearing of this application, Mr. Goldberg was examined by counsel for Laserworks pursuant to section 163(2) of the B.I.A. This examination was by consent.

12 Upon the examination Mr. Goldberg testified that he had sent faxes to some of the creditors of Laserworks (but not all) seeking to purchase their claims on behalf of 3004876 Nova Scotia Limited (the "numbered company"). Each of these faxes was similar, but not all were the same. In most cases a telephone call preceded the fax. Mr. Goldberg agreed to provide a summary detailing the offers made and this was produced prior to the hearing of this application.

13 It would appear from the summary that the offers made to creditors varied in some degree, with those creditors with smaller claims generally being offered a higher percentage of their claim. Eighteen creditors delivered their proxy, and the vast majority also delivered an assignment agreement. The assignment agreements were not executed by the numbered company. It seems that this was an attempt to avoid a consolidation of the claims into one claim for the purpose of voting. The numbered company through Mr. Goldberg clearly wished to be able to vote both the value of the claims, and individually on behalf of each assigning creditor. In this regard, Mr. Goldberg testified that it was a condition of payment that the creditor both return the assignment and proxy, and that the claim be proven. The creditors were only to be paid on proven claims. Notwithstanding this it does appear from the summary provided that at least four creditors were paid on their claims.

14 Mr. Goldberg testified that he was acting for more than one client. Objection was taken to revealing who the client was on the basis of solicitor client privilege. This objection was withdrawn, and Mr. Goldberg revealed that the numbered company was a "shelf" company, and that his client was Datarite Inc. ("Datarite"). Mr. Goldberg's instructions came from Datarite. He testified that one of Datarite's divisions was a business competitor of Laserworks.

Decision

15 Moving to the two applications before me, I will first deal with the four claims to which Mr. Goldberg objects.

The "Goldberg" Objections

16 There is no record of any notice being given to any of these four creditors of this application. It is trite to say that they are entitled to participate on the application insofar as the adjudication of their claims is concerned. This being the case, I decline to take the matter of this objection any further at this time. Mr. Goldberg's client shall have ten days from the date of this decision to make further application on notice to the affected creditors, failing which the chairperson should consider the objections withdrawn and proceed accordingly.

17 I now turn to the issue of the eighteen claims represented by Mr. Goldberg's proxies.

The "Laserworks" Objections

18 I am satisfied that the appropriate parties are before me on this application. Counsel for the numbered company was present and indeed provided an extensive written brief. The eighteen creditors have given their proxies to Mr. Goldberg (as

solicitor for the numbered company) and essentially assigned their rights to the numbered company. The trustee had notice and was represented.

19 I am indebted to counsel for the numbered company, for Laserworks, and for the trustee, for their very well reasoned pre-hearing memoranda. It is useful to summarize those submissions.

20 Counsel for the numbered company concedes that the court has an inherent supervisory jurisdiction in bankruptcy. An example of this is the practice of the court to strike down secret agreements between a debtor and creditor. Another example is the ability of the court to interfere with decisions of inspectors. In the former case secret agreements are struck down as being essentially a fraud upon the general body of creditors. In the latter case, the supervisory function of the court arises from the position of inspectors as fiduciaries. Counsel argues that neither principle extends to agreements between creditors, who are not fiduciaries and who are entitled to act entirely in their own self interest.

21 Counsel for the numbered company goes on to argue that the motive of a creditor in voting is irrelevant so long as the creditor has satisfied the technical requirements in filing a proof of claim and otherwise complying with the provisions of the B.I.A. Counsel cites *Teac Canada Ltd. c. Bédard Louis Inc.* (1991), 22 C.B.R. (3d) 218 (C.A. Que.), a case from the Quebec Court of Appeal, for the proposition that while a creditor may have a conflict of interest, such a conflict would not deny the creditor the ability to vote its claim. I would simply note that the circumstances in *Teac Canada Ltd.* were entirely different to those in this case and the same result should not necessarily follow.

22 Counsel for Laserworks refers the court to the following extract from Houlden and Morawetz, *Bankruptcy and Insolvency Law of Canada*, at p. 2-144.3 (looseleaf):

> In deciding whether the proposal should be approved, the court must take the following interests into account: (a) the interests of the debtor in making a settlement with creditors; (b) the interests of creditors in procuring a settlement which is reasonable and which does not prejudice their rights; and (c) the interests of the public in the fashioning of a settlement which preserves the integrity of the bankruptcy process and complies with the requirements of commercial morality.

23 Counsel argues that while these considerations are germane to an application to approve a proposal, they should also be relevant in the circumstances present in this case. As a matter of public policy the court should not condone the activities of Datarite here.

24 To this I would say that it is only in rare cases that a court, and particularly the Registrar of the court, should succumb to the temptation to rest an otherwise just result simply on the coat hanger of public policy.

25 Counsel for the trustee offers support to counsel for Laserworks in this public policy submission. He says that just as secret dealings between a debtor and creditor should be frowned upon, so too should secret dealings between creditors in circumstances such as this. Counsel submits that the court has a general supervisory function in respect to the voting process, and while there is no law prohibiting a creditor voting in his or her own best interest absent abuse, where abuse is present the court may intervene.

26 Before turning to deal with these submissions, it is essential that I make some findings of fact. In large part the facts are uncontested. No affidavits were filed, but counsel agree that I may rely on the minutes of the meeting of creditors, the testimony of Mr. Goldberg upon the section 163(2) examination, and the list provided by Mr. Goldberg in compliance with his undertaking on the examination.

27 I find that Datarite through its solicitor approached some but not all of the creditors of Laserworks with the intention of obtaining an assignment of those creditors' claims and consequently rights to vote on the proposal. The claims were obtained and the votes utilized to defeat the proposal. This would have the effect under section 57(a) of the B.I.A. of placing Laserworks into bankruptcy by virtue of a deemed assignment.

28 I can only conclude that the purpose of Datarite was to effect the bankruptcy of Laserworks. It is a reasonable supposition that the purpose was to remove a competitor from the marketplace. I find that it was the intention of Datarite to place Laserworks in bankruptcy.

29 I further find that the motive was to lessen competition.

30 In my view, Datarite was engaged throughout in an improper purpose not contemplated by the B.I.A., the purpose of which is far removed from the use to which Datarite put it.

31 Where the court is satisfied that a creditor is acting to place the debtor in bankruptcy for an improper purpose, does the court have the ability to prevent this abuse of the provisions of the B.I.A.? If it does, does this ability extend to the Registrar or is it confined to a Supreme Court Justice exercising his or her bankruptcy jurisdiction?

32 In this province the Supreme Court is vested with jurisdiction both at law and in equity so as to enable the court to exercise original, auxiliary and ancillary jurisdiction in bankruptcy: B.I.A., section 183(1).

> It is well established law that nothing shall be intended to be out of the jurisdiction of a Superior Court but what expressly appears to be so. The jurisdiction of the king's Superior Courts over matters cognizable by them can not be taken away but by express words or perhaps by necessary implication arising from the use of words absolutely inconsistent with the exercise of the jurisdiction, or to which effect can not be given except by exclusion of such jurisdiction. If a court has jurisdiction of the principle matter it has also jurisdiction over all matters incident thereto and may try them according to the course of their law so that it be not contrary to the common law. I realize that the Bankruptcy law is statutory mainly and a Court should not go beyond the provisions of the statute applicable. But, if the subject-matter is within the statute, the Court may draw on its inherent powers to give effect to the provisions of the statute ... it seems quite clear to me that the absence of any specific rule should not render the Court incapable of exercising its jurisdiction.
>
> *Loxtave Buildings of Canada, Ltd., Re* (1943), 25 C.B.R. 22 (Sask.Q.B.), at p. 25.

33 Section 2 of the B.I.A. defines the "court" to include a Registrar when exercising the powers of the court conferred on a Registrar under the Act. Section 192(1)(h) gives the Registrar jurisdiction to hear and determine matters relating to proofs of claim, whether or not opposed. I conclude therefore that on this application I may exercise the jurisdiction of the court in its totality.

34 I agree with the submissions of counsel for all the parties that there are instances where the court acting under what might be described as its inherent jurisdiction may prescribe an activity on the part of an interested party to a bankruptcy notwithstanding the lack of a statutory prohibition. In this case counsel for Laserworks commends to the court the principles set out in cases such as *McKewan v. Sanderson* (1873), L.R. 15 Eq. 229 (Eng. V.-C.), *Sadler Manufacturing Co. v. Golt* (1954), 35 C.B.R. 67 (C.S. Que.), and *Newlands Textiles Inc. v. Carrier* (1983), 47 C.B.R. (N.S.) 148 (Ont. S.C.), dealing with the situation where by virtue of a secret agreement with the debtor a creditor obtains a benefit not available to the general body of creditors. Such secret agreements will not be enforced.

35 In my view it is a quantum leap from that principle to some general principle that secret agreements between creditors should not be enforced, and that further the court should actively intervene to substitute its perception of what is appropriate in any particular circumstance. This is a leap I am not prepared to take.

36 This, however, does not end the analysis.

37 It has long been held that the court will not grant a petition in bankruptcy where the petition is filed for an improper purpose: *Re De La Hooke* (1934), 15 C.B.R. 485 (Ont. S.C.), *Re Pappy's Good Eats Ltd.* (1985), 56 C.B.R. (N.S.) 304 (Ont. S.C.), *Dimples Diapers Inc. v. Paperboard Industries Corp.* (1992), 15 C.B.R. (3d) 204 (Ont. Gen. Div.), *Re Shepard* (1996), 40 C.B.R. (3d) 145 (Man. Master).

38 In *Hooke* the petitioner obtained an assignment of a judgment against the debtor for the sole purpose of filing a petition in bankruptcy and of removing the debtor as a business competitor. In that case, as is the situation in this case, there was no evidence that the debtor had any business dealings with the party seeking to place the debtor in bankruptcy. The petition was dismissed.

39 In *Hooke* the court made extensive reference to the decision of the House of Lords in *King v. Henderson*, [1898] A.C. 720 (New South Wales P.C.). The comments of James, L.J., at p. 732, are particularly germane here:

> After what Lord Justice Cotton has said, in which I entirely agree, people will probably think twice before they buy debts for the purpose of taking bankruptcy proceedings.

40 Lord Justice Cotton had commented that the proceedings in bankruptcy were not taken to obtain payment of the debt, but rather the debt was purchased for the purpose of taking the proceedings. I would simply add that in light of the decision I make here persons should certainly think twice before they purchase debts in order to defeat a proposal.

41 It is my opinion that the eighteen creditors are tainted with the improper motive of Datarite. In *Pappy's Good Eats* the petition was filed by a creditor with a genuine claim. The creditor entered into an agreement with three franchisees of the debtor. This agreement provided that the creditor would prosecute the bankruptcy proceeding while the franchisees financed the proceeding in exchange for a share in the dividends. The motive of the franchisees was to bring about a bankruptcy so as to terminate the franchise agreements between them and the debtor.

42 The court found that there had been an improper use of the bankruptcy legislation. The effect of the agreement was to embroil the creditor in the improper objectives of the franchisees who were intermeddling in the proceeding. This tainted the whole proceeding. Clearly where the object of the intermeddling party is to bring about the bankruptcy of the debtor an improper purpose is present. The court will act to prevent such an abuse of the legislation.

43 The other cases I have referred to, *Dimples Diapers Inc.*and *Shepard* also deal with bankruptcy petitions instigated for an improper collateral purpose. In *Dimples* that purpose was to recover a trademark and a business opportunity. In *Shepard* that purpose was to obtain control of certain shares.

44 While this case does not involve a bankruptcy petition, it does involve the placing of Laserworks into bankruptcy. In my view, it would be wrong to allow Datarite to do in the proposal process what it could not do by petition. Datarite's intention was to place Laserworks in bankruptcy. The motive was to remove a competitor. That motive reveals an improper purpose. The court will not allow to be done by the back door what may not be done by the front.

45 By entering into this arrangement with the numbered company the eighteen creditors have tainted themselves and become embroiled in the improper purpose of Datarite. Their votes cannot stand. If Laserworks has the right to be free of this type of interference the Court must be able to fashion a remedy. This court does have the inherent jurisdiction to supervise the bankruptcy process and consequently the conduct of creditors where that conduct constitutes an abuse of the provisions of the B.I.A. While creditors can certainly vote in their own best interest, they may not collude with a third party to place a debtor in bankruptcy for an improper purpose. Such activity lacks commercial morality and offends the integrity of the bankruptcy process.

46 The objection to the votes of the eighteen creditors is sustained. The chairperson of the meeting is directed to tabulate the votes without regard to the votes of the eighteen creditors in question, and to proceed according to the result. As matters stand, this will apparently result in the approval of the proposal.

47 My decision here should not be taken as a denial of the rights of the eighteen creditors to share in the dividends payable under the proposal. They may do so.

48 Given my findings with respect to the intent and motive of Datarite, I find it unnecessary to consider whether Datarite should have exercised one vote or eighteen.

49 While the activities of Datarite were novel in respect to a proposal, it seems to me clear that Datarite could only be aware that its purpose was improper. Thus this is an appropriate case for costs. I award costs against Datarite in favour of Laserworks in the amount of $1,000.00, and in favour of the trustee in the amount of $1,000.00.

Application granted.

TAB 2

COURT OF APPEAL FOR ONTARIO

CITATION: Nortel Networks Corporation (Re), 2016 ONCA 332
DATE: 20160503
DOCKET: M45307, M45309, M45310
M45311, M45312, M45313

Hoy A.C.J.O, and Blair and Pepall JJ.A.

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

Application under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended

Sheila Block, Scott A. Bomhof, Andrew Gray, Adam M. Slavens and Jeremy Opolsky, for the moving parties, the U.S. Debtors[1]

Richard B. Swan, S. Richard Orzy and Gavin H. Finlayson, for the moving party, the Ad Hoc Group of Bondholders

David R. Byers and Daniel S. Murdoch, for the moving party, the Conflicts Administrator of Nortel Networks S.A.

Shayne Kukulowicz, Michael Wunder, Ryan Jacobs, Geoffrey Shaw and Jane Dietrich, for the moving party, the Official Committee of Unsecured Creditors of Nortel Networks Inc. *et al.*

Andrew Kent, Brett Harrison and Laura Brazil, for the moving party, The Bank of New York Mellon as Indenture Trustee

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[1] The U.S. Debtors are Nortel Networks Inc. (formerly Northern Telecom International), Nortel Networks Capital Corporation, Nortel Altsystems Inc., Nortel Altsystems International Inc., Xros, Inc., Sonoma Systems, Qtera Corporation, CoreTek, Inc., Nortel Networks Applications Management Solutions Inc., Nortel Networks Optical Components Inc., Nortel Networks HPOCS Inc., Architel Systems (U.S.) Corporation, Nortel Networks International Inc., Northern Telecom International Inc., Nortel Networks Cable Solutions Inc. and Nortel Networks (CALA) Inc.

Steven L. Graff, Ian Aversa and Miranda Spence, for the moving party, the Nortel Trade Claims Consortium

Michael E. Barrack, D.J. Miller, John L. Finnigan, Michael S. Shakra and Andrea McEwan, for the responding parties, the Board of the Pension Protection Fund and Nortel Networks U.K. Pension Trust Ltd.

Benjamin Zarnett, Jessica Kimmel, Peter Ruby and Peter Kolla, for the responding party, the Monitor, Ernst & Young Inc.

Kenneth Kraft and John Salmas, for the responding party, Wilmington Trust, National Association

Derrick Tay and Jennifer Stam, for the responding parties, the Canadian Debtors[2]

Kenneth Rosenberg, Lily Harmer and Massimo Starnino, for the responding party, the Superintendent of Financial Services as Administrator of the Pension Benefits Guarantee Fund

Mark Zigler and Ari Kaplan, for the responding parties, the Former Employees of Nortel and LTD Beneficiaries

Arthur O. Jacques, Paul Steep and Byron Shaw, for the responding party, the Canadian Creditors' Committee

Barry E. Wadsworth, for the responding party, CAW-Canada

Matthew P. Gottlieb and Matthew Milne-Smith, for the responding parties, the Joint Administrators of the EMEA Debtors[3] other than Nortel Networks S.A.

Heard: In Writing

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[2] The Canadian Debtors are Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Technology Corporation, Nortel Networks Global Corporation, and Nortel Networks International Corporation.

[3] The EMEA Debtors are Nortel Networks UK Limited, Nortel Networks S.A., Nortel Networks (Ireland) Limited, Nortel GmbH, Nortel Networks (Austria) GmbH, Nortel Networks AB, Nortel Networks BV, Nortel Networks Engineering Service Kft, Nortel Networks France S.A.S., Nortel Networks Hispania, S.A., Nortel Networks International Finance & Holding BV, Nortel Networks NV, Nortel Networks OY, Nortel Networks Polska Sp. z.o.o., Nortel Networks Portugal SA, Nortel Networks Romania SRL, Nortel Networks SpA, Nortel Networks Slovensko, s.r.o., and Nortel Networks, s.r.o.

Motions for leave to appeal from the judgment of Justice Frank J.C. Newbould of the Superior Court of Justice, dated May 12, 2015 and July 6, 2015, with reasons reported at 2015 ONSC 2987, 27 C.B.R. (6th) 175, and 2015 ONSC 4170, 27 C.B.R. (6th) 51.

BY THE COURT:

A. INTRODUCTION

[1] January 14, 2009 was not a good day. At that time, Nortel Networks Corp. (“NNC”) and the other Nortel Canadian Debtors filed for insolvency protection under the *Companies Creditors’ Arrangement Act*, R.S.C. 1985, c. C-36 (“*CCAA*”). That same day, Nortel Networks Inc. (“NNI”) and other U.S. Debtors filed voluntary petitions for relief under Chapter 11 of the U.S. *Bankruptcy Code*, 11 U.S.C. §§1101 – 1174, and other Nortel entities incorporated in Europe, the Middle East and Africa (“EMEA”) were placed under administration in England by the High Court of England and Wales under the U.K. *Insolvency Act 1986*, c. 45. Shortly afterwards, courts in Canada and the United States approved a cross-border, court-to-court protocol that established procedures for the co-ordination of cross-border proceedings in Canada and the U.S.

[2] More than seven years later, many Januarys have come and gone and these insolvency proceedings continue. During that time:

- more than 6,800 Nortel former employees or pensioners have died;
- well in excess of $1 billion has been incurred in costs; and

- Nortel's assets have been sold and some $7.3 billion[4] in sale proceeds have been placed in escrow (the "Lockbox Funds").

[3] The leave motions now before this court arise from the joint trial dealing with the allocation of the Lockbox Funds. Newbould J. (the "trial judge) of Ontario's Superior Court of Justice (Commercial List) and Judge Gross of the U.S. Bankruptcy Court for the District of Delaware presided over the joint trial.[5] It was held over the course of six weeks. Each judge rendered separate decisions on May 12, 2015. Each concluded that the Lockbox Funds should be allocated on a *pro rata* basis among the various Nortel debtor estates. Although their analysis differed somewhat, the outcome was the same.

[4] Appeal proceedings were initiated in Canada and the U.S. The moving parties were authorized to file their leave materials in the absence of an issued judgment on the basis that counsel would subsequently file the formal judgment. The formal judgment was issued on April 26, 2016 and filed with this court on April 27, 2016.

[5] Before this court, the six moving parties, led by the U.S. Debtors, seek leave to appeal the trial judge's judgment pursuant to s. 13 of the *CCAA*. They submit that the trial judge made fundamental errors and that the proposed appeal

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[4] All references to dollars are to U.S. dollars, unless otherwise specified.
[5] Judge Gross's reasons are reported at 532 B.R. 494 (2015).

is of significance to the practice of insolvency and to the parties, and will not delay the completion of the *CCAA* proceedings.

[6] The responding parties, led by the Board of the Pension Protection Fund and Nortel Networks UK Pension Trust Limited ("UKPC"), submit that the record supports the trial judge's factual findings, which were integral to his analysis, including his findings that Nortel's assets were jointly created, that the Nortel group of companies operated on a fully-integrated global basis and that Nortel did not operate separate businesses in separate countries. In their submission, the proposed appeal is not *prima facie* meritorious. In addition, the remaining elements of the test for leave to appeal under the *CCAA* have not all been met.

[7] After consideration of each of the factums[6] and other materials filed on the leave motions, we agree with the responding parties that the test for leave has not been met. For the reasons that follow, we dismiss the moving parties' motions for leave to appeal.

B. GENESIS OF DISPUTE

[8] NNC was a publicly-traded Canadian corporation at the helm of a global networking solutions and telecommunications business, and the direct or indirect

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[6] In accordance with the directions of the Court of Appeal case management judge, there was one main factum filed on behalf of the moving parties by the U.S. Debtors and one main factum filed on behalf of the responding parties by the UKPC. Six supplementary factums and one reply factum were also filed.

parent of more than 130 subsidiaries located in more than 100 countries. These companies were collectively referred to as the “Nortel Group” or “Nortel”.

[9] NNC was the successor to a long line of companies, headquartered in Canada, that date back to the founding of the Bell Telephone Company of Canada in 1883. NNC’s principal, direct operating subsidiary was Nortel Networks Limited (“NNL”), also a Canadian company. NNL was the direct or indirect parent of operating companies located around the world. It owned 100 percent of the equity of each of the following entities: NNI, Nortel’s operating company in the United States; Nortel Networks UK Ltd. (“NNUK”), Nortel’s operating company in the United Kingdom; and, Nortel Networks (Ireland) Ltd. (“NN Ireland”), Nortel’s operating company in Ireland. It also owned 91.17 per cent of the equity of Nortel Networks S.A. (“NNSA”), Nortel’s operating company in France.

[10] Following the insolvency filings, Nortel’s initial plan was to downsize and carry on portions of the telecommunications business. However, by June 2009, the decision was made to liquidate Nortel’s assets.

[11] On June 29, 2009, an Interim Funding and Settlement Agreement (“IFSA”) was approved by both the Canadian and American courts. Among other things, it addressed interim funding for NNL and the anticipated sales of Nortel’s business lines and residual intellectual property (“IP”). The parties, consisting of

the Canadian Debtors, the U.S. Debtors[7], and the EMEA Debtors[8], agreed to cooperate with the sales process and also agreed that the proceeds of sale would be held in escrow. The issue of allocation was deferred.

[12] Under the IFSA, there would be no distribution out of escrow without "either (i) agreement of all of the Selling Debtors[9] or (ii) … determination by the relevant dispute resolver(s) under the terms of the Protocol … applicable to the Sale Proceeds". The parties were then to negotiate and attempt to reach agreement "on a protocol for resolving disputes concerning the allocation of Sale Proceeds from Sale Transactions (the "Interim Sales Protocol")". Despite numerous attempts at resolution, agreement on both an Interim Sales Protocol and allocation proved to be elusive.

[13] Meanwhile, over $7 billion was generated from various asset sales and other realizations. From mid-2009 until March 2011, proceeds of $3.285 billion were generated from the sale of Nortel's various business lines, including some patents. Of that amount, $2.85 billion is available for allocation. In June 2011, proceeds of approximately $4.5 billion were generated from the sale of Nortel's residual intellectual property, consisting of approximately 7,000 patents and

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[7] With the exception of Nortel Networks (CALA) Inc.

[8] The Joint Administrators were also party to the IFSA but only for the purposes of Section 17 (No Personal Liability of the Joint Administrators).

[9] A description of "Selling Debtor" is found in s.12 (a) of the IFSA: "Each Debtor hereby agrees that its execution of definitive documentation with a purchaser (or, in the case of any auction, the successful bidder in any such auction) of, or closing of any sale of, material assets of any of the Debtors to which such Debtor (a "Selling Debtor") is proposed to be a party…"

patent applications, to the Rockstar consortium. In total, approximately $7.3 billion is currently held in escrow.

[14] By orders dated January 21, 2010, the Canadian and U.S. courts approved a "Final Canadian Funding and Settlement Agreement". The Agreement addressed a number of issues and allowed NNI a $2 billion claim against NNL in NNL's *CCAA* proceeding, which claim is not subject to offset or counterclaims.

[15] The parties still could not agree on an Interim Sales Protocol or on allocation. In the spring of 2013, the Canadian court and the U.S. bankruptcy court granted orders approving an "Allocation Protocol". The purpose of this Protocol was to set out "binding procedures for determining the allocation of the Sale Proceeds among the Selling Debtors"[10]. It provided for a joint hearing to determine allocation before the Canadian court and the U.S. bankruptcy court.[11] Any party in interest was at liberty to advance any theory on allocation. Leave to appeal that order was denied by this court on June 20, 2013.

[16] The issue of allocation of the Lockbox Funds then proceeded to trial.

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[10] Selling Debtors was defined in the Allocation Protocol as the "Canadian Debtors, U.S. Debtors, EMEA Debtors and Nortel Networks Optical Components Ltd., Nortel Networks AS, Nortel Networks AG, Nortel Networks South Africa (Pty) Limited, and Nortel Networks (Northern Ireland) Limited."

[11] The EMEA Debtors were held to have attorned to the jurisdiction of the Canadian court and the U.S. bankruptcy court.

C. TRIAL JUDGE'S DECISION

(1) Trial Decision

[17] The trial judge's reasons may be summarized. He commenced by reviewing the history of the Nortel Group. He described the operations and the four main product groups or lines of business. Before turning to his analysis of the legal issues, he made a number of important findings about the Nortel Group's structure. He found, and repeatedly reiterated, that the Nortel Group operated as a highly-integrated multinational enterprise. For instance, he stated:

> [16] The Nortel Group operated along business lines as a highly integrated multinational enterprise with a matrix structure that transcended geographic boundaries and legal entities organized around the world. Each entity, such as NNL, NNI, NNUK, NN Ireland and NNSA, was integrated into regional and product line management structures to share information and perform research and development ("R&D"), sales and other common functions across geographic boundaries and across legal entities. The matrix structure was designed to enable Nortel to function more efficiently, drawing on employees from different functional disciplines worldwide, allowing them to work together to develop products and attract and provide service to customers, fulfilling their demands globally.
>
> [17] As a result of Nortel's matrix structure, no single Nortel entity, either NNL or any of the other Canadian debtors in Canada, NNI or any of the other US debtors in the United States or NNUK or any of the other EMEA debtors, was able to provide the full line of Nortel products and services, including R&D capabilities, on a stand-alone basis. While Nortel ensured that all corporate entities complied with local laws regarding

corporate governance, no corporate entity carried on business on its own.

[18] The trial judge also found that R&D, which was performed at labs around the world, was the primary driver of Nortel's value and profit.

[19] After reviewing the necessary background, the trial judge turned to the legal issues before him, starting with the interpretation of the Master Research and Development Agreement ("MRDA"). The MRDA dealt with transfer-pricing arrangements, effective from 2001 onwards, among NNL, NNI, NNUK, NNSA and NN Ireland, who were parties to the agreement.[12]

[20] The parties took differing and competing positions on the meaning and application of the MRDA:

- The Monitor (on behalf of the Canadian Debtors), supported by the Canadian Creditors' Committee ("CCC"), took the position that under the MRDA, NNL owned the IP whereas other participants to the MRDA were simply licensees. They argued that the proceeds derived from the sale of the residual IP belonged exclusively to NNL.
- The U.S. Debtors and other U.S. interests, including the Bondholders, argued that NNI and the other licensees held all of the rights and value in the IP in their respective exclusive territories as defined in the MRDA.
- The EMEA Debtors asserted that parties to the MRDA jointly owned all of the IP in proportion to their financial contributions to R&D and that all

[12] Nortel Networks Australia was also a party to the agreement. It ceased being a Residual Profit Entity on December 31, 2007.

should share in the sale proceeds attributable to IP in those same proportions. The joint ownership arose independent of, but was recognized in, the MRDA.

- The UKPC took the position that the MRDA should not govern allocation and that a *pro rata* allocation based on a *pari passu* distribution should be used. The CCC also adopted this as its alternative position.

[21] The trial judge found that, by its terms, the MRDA was to be construed in accordance with, and governed by, Ontario law. He reviewed the applicable principles of contractual interpretation, including the law on factual matrix (surrounding circumstances), commercial reasonableness, and recitals. In reviewing the law, he considered the recent authority from the Supreme Court of Canada on contractual interpretation, *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633, which was released during the course of the trial. He considered in detail the parties' positions, the language of the MRDA and evidence on factual matrix.

[22] He concluded that the MRDA was an operating agreement and was not intended to, nor did it, deal with the disposal of all of Nortel's assets in a situation in which no revenue was being earned and no profits or losses were occurring. Rather, he found that the MRDA was developed for, and driven by, transfer-pricing concepts for tax purposes and did not govern allocation after Nortel ceased operations:

> [177] I accept that the MRDA was a transfer pricing document created for tax purposes. The licenses were a part of it. The licenses granted under it were never dealt with separately from the MRDA. Their only purpose was to support the intended tax treatment resulting from the MRDA.
>
> …
>
> [185] I conclude that the circumstances surrounding the creation of the MRDA lead to no other result but that the construct of legal title to the NN Technology being in NNL in return for NNL granting exclusive licenses to the Licensed Participants was only for the purpose of supporting the proposed method to split profits or losses on a tax efficient basis while Nortel operated as a going concern business. The agreement in its application was intended to apply only to Nortel while it operated and not to deal with rights after Nortel and its subsidiaries stopped operating its businesses.

[23] Thus, he rejected the primary positions of the Monitor, the CCC, the U.S. Debtors and other U.S. interests, as well as the EMEA Debtors' joint ownership theory.

[24] Having found that the MRDA did not govern allocation on Nortel's insolvency and having rejected the joint ownership theory, the trial judge turned to the metric to be used to allocate the Lockbox Funds. He found that the intangible assets that were sold were not separately located or owned in any one jurisdiction. Rather, they were created by all of the so-called "Residual Profit Entities" or "RPEs" (namely, NNL, NNI, NNUK, NNSA and NN Ireland), which were located in different jurisdictions. In addition, the matrix structure allowed

Nortel to draw on employees from different functional disciplines worldwide, regardless of region or country, according to need.

[25] He held that NNL was not entitled to the proceeds of sale simply because the patents were in its name:

> [197] This was not one corporation and one set of employees inventing IP that led to patents. Nortel was a highly integrated multi-national enterprise with all RPEs doing R&D that led to patents being granted. It was R&D that drove Nortel's business. R&D and the intellectual property created from it was the primary driver of Nortel's value and profits. All parties agree on that. It would unjustly enrich NNL to deprive all of the other RPEs of the work that they did in creating the IP just because the patents were registered in NNL's name.

[26] He determined that he had wide powers under the *CCAA* to do what was just in the circumstances. Section 11 of the *CCAA*, which reflected prior jurisprudence, expressly provides that a court may make any order it considers appropriate in the circumstances, subject to the provisions of the Act. He wrote:

> [208] In this case, insolvency practitioners, academics, international bodies, and others have watched as Nortel's early success in maximizing the value of its global assets through cooperation has disintegrated into value-erosive adversarial and territorial litigation described by many as scorched earth litigation. The costs have well exceeded $1 billion. A global solution in this unprecedented situation is required and perforce, as this situation has not been faced before, it will by its nature involve innovation. Our courts have such jurisdiction. [Footnote omitted.]

[27] He observed that it is a fundamental tenet of insolvency law that all debts be paid *pari passu* and that all unsecured creditors receive equal treatment. In his view, a *pro rata* allocation could be achieved by directing an allocation of the Lockbox Funds to each Debtor Estate based on the percentage that the claims against that Estate bore to the total claims against all of the Debtor Estates.

[28] In reaching this conclusion, the trial judge dealt with the argument that a *pro rata* allocation would amount to substantive consolidation. He concluded that a *pro rata* allocation would not constitute substantive consolidation in the unique circumstances of this case. In any event, even if it were substantive consolidation, there was precedent that justified substantive consolidation in this case: *Re Lehndorff General Partner Ltd.* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div.); *Re PSINet Ltd.* (2002), 33 C.B.R. 4th 284 (Ont. S.C.J.); *Re Northland Properties Ltd.* (1988), 29 B.C.L.R. (2d) 257 (S.C.).

[29] Ultimately, he concluded that the Lockbox Funds were to be allocated on a *pro rata* basis in accordance with certain governing principles, which are outlined below.

[30] After his reasons were released, the U.S. Debtors supported by the Official Committee, the Ad Hoc Group of Bondholders and the Law Debenture Trust Company of New York filed motions for clarification, reconsideration or amendment in Canada and the U.S. and a number of points were clarified.

[31] In the end result, the judgment that was signed, issued and entered on April 26, 2016 provided that the allocation proceed on a *pro rata* basis in accordance with the following principles:

> (a) Each Debtor Estate[13] is to be allocated that percentage of the Lockbox Funds that the total allowed pre-filing claims against that Debtor Estate bear to the total allowed pre-filing claims against all Debtor Estates.
>
> (b) In determining what the claims are against the Debtor Estates, pre-filing claims of the kind provable under the *Companies' Creditors Arrangement Act* that have received court approval and which have been paid may be taken into account to the extent that they have been paid under the settlement.
>
> (c) In determining what the pre-filing claims are against each Debtor Estate, a claim that can be made against more than one Debtor Estate can only be calculated and recognized once.
>
> i. Claims on bonds are to be made on the Debtor Estate of the issuer and shall be included in that Debtor Estate's total allowed claims for the purpose of determining its allocation. A claim can be recognized by the Debtor Estate that guaranteed the bond, but those claims will not be taken into account in determining the claims against the Debtor Estates for allocation purposes.
>
> ii. If the UK Pension Claimants make a claim for the approximately £2.2 billion deficit in the NNUK pension plan against NNUK and also against other EMEA Debtors or the EMEA Non-Filed

[13] The order defines "Debtor Estate" as "each of the individual legal entities" set out in Schedule B. Schedule B lists the 45 entities, including the Canadian Debtors, the U.S. Debtors, the EMEA Debtors and five "EMEA Non-Filed Entities" who have not commenced insolvency proceedings. See also the similar definition given to Selling Debtors under the Allocation Protocol.

> Entities, the claim against NNUK will be taken into account in determining claims against the Debtor Estates for allocation purposes but the additional claims against the EMEA Debtors or the EMEA Non-Filed Entities will not be taken into account in determining the claims against the Debtor Estates for allocation purposes.
>
> (d) Subject to the general proviso in (c), above, in respect of claims that can be made against more than one Debtor Estate, pre-filing intercompany claims against a Debtor Estate shall be included in the determination of the claims against that Debtor Estate for purposes of its allocation.
>
> (e) The following specific pre-filing claims shall be included in the determination of the allowed claims against NNL for purposes of determining its allocation:
>
> i. the US$2.0627 billion claim of NNI against NNL that was approved by this Court and the U.S. Court;
>
> ii. the claims of NNUK and Nortel Networks SpA against NNL pursuant to the Agreement Settling EMEA Canadian Claims and Related Claims dated July 9, 2014; and
>
> iii. the claim of the UK Pension Claimants against NNL recognized in this Court's judgment of December 9, 2014, as such claim is finally determined.
>
> (f) Cash on hand in any Debtor Estate will not be taken into account in determining its allocation. Each Debtor Estate with cash on hand will continue to hold that cash and deal with it in accordance with its administration.

D. ANALYSIS

[32] Six moving parties now seek leave to appeal from the trial judge's allocation decision: the U.S. Debtors, the Ad Hoc Group of Bondholders, the

Conflicts Administrator of Nortel Networks S.A., the Official Committee of Unsecured Creditors of NNI and others, the Bank of New York Mellon as Indenture Trustee, and the Nortel Trade Claims Consortium.

[33] We will commence our analysis by discussing the test for leave to appeal under the *CCAA* and then address the moving parties' positions in relation to that test.

(1) Test for Leave to Appeal

[34] Section 13 of the *CCAA* provides that any person dissatisfied with an order or a decision made under the Act may appeal from the order or decision with leave. Leave to appeal is granted sparingly in *CCAA* proceedings and only where there are serious and arguable grounds that are of real and significant interest to the parties. In addressing whether leave should be granted, the court will consider whether:

> (a) the proposed appeal is *prima facie* meritorious or frivolous;
>
> (b) the points on the proposed appeal are of significance to the practice;
>
> (c) the points on the proposed appeal are of significance to the action; and
>
> (d) whether the proposed appeal will unduly hinder the progress of the action.

See, for e.g.: *Re Stelco Inc.* (2005), 75 O.R. (3d) 5 (C.A.), at para. 24; *Re Timminco Ltd.*, 2012 ONCA 552, 2 C.B.R. (6th) 332, at para. 2; and *Re Nortel Networks Corp.*, 2013 ONCA 427, 5 C.B.R. (6th) 254, at para. 3.

(a) Whether Appeal is *Prima Facie* Meritorious

[35] The moving parties take the position that leave should be granted because the appeal is *prima facie* meritorious. In making that argument, they raise three main issues – substantive consolidation, the interpretation of the MRDA, and questions of fairness. We will deal with each issue in turn.

(i) Substantive consolidation

Position of the Moving Parties

[36] First, the moving parties submit that the trial judge erred in not recognizing that the allocation ordered departed from “corporate separateness” and was a form of substantive consolidation.

[37] Secondly, it is alleged that the trial judge erred by applying an inappropriately low threshold for the application of substantive consolidation.

[38] In its supplementary factum, the Bank of New York Mellon, as Indenture Trustee, makes a related argument. It submits that since the Nortel proceeding no longer involves a restructuring, the *CCAA*’s purpose is spent and the proceeds should thereafter be distributed under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (“*BIA*”), or at least in a manner consistent with the *BIA*

scheme. It says the *BIA* does not contemplate consolidation but rather distribution on an entity-by-entity basis.

[39] Finally, the Ad Hoc Group of Bondholders makes a related argument. It submits that the allocation decision takes property interests that belong to certain debtor estates and gives them to others. They argue that, even though the authority provided under s. 11 is broad, the *CCAA* does not permit a court to redistribute property in this way.

Analysis

[40] The moving parties' arguments on substantive consolidation are not *prima facie* meritorious.

[41] Professor Janis Sarra, a leading expert on insolvency law in Canada, describes substantive consolidation in her article "Corporate Group Insolvencies: Seeing the Forest and the Trees" (2008) 24 B.F.L.R. 63, at pp. 80 - 81:

> Substantive consolidation essentially treats member entities of a corporate group as one entity. In the context of liquidation, it creates a common pool of assets to meet creditors' claims. In the context of restructuring, it may create the opportunity for creditors to share in the future upside potential of a restructured entity or entities by centralizing and negotiating an arrangement in respect of their claims. Canadian courts have recognized substantive consolidation under both the *BIA* and the *CCAA* where there is evidence of intertwined assets and liabilities; integrated administrative functioning and operations; a perception by creditors that they are dealing with an integrated entity; common control and governance structures;

> where it would be impracticable to separate the affairs of related entities; where it is more cost effective and beneficial to creditors to have the proceedings administered as a single estate; and where it would result in an expeditious and administratively efficient administration of the proceeding.

[42] As we have noted, the trial judge concluded that *pro rata* allocation was appropriate, that it did not amount to substantive consolidation, and that even if it could be said that a *pro rata* allocation involved substantive consolidation, it was not precluded by law in the unique circumstances of the case.

[43] In reaching those conclusions, he made numerous factual findings, in addition to those already mentioned, including the following:

- "Nortel (a) had fully integrated and interdependent operations; (b) had intercompany guarantees for its primary indebtedness; (c) operated a consolidated treasury system in which generated cash was used throughout the Nortel Group as required; (d) disseminated consolidated financial information throughout its entire history, save for the year before its bankruptcy; and (e) created IP through integrated R&D activities that were global in scope": para. 223.
- "[N]o one entity or region was able to provide the full line of Nortel products and services": para. 202.
- "Nortel's matrix structure also allowed Nortel to draw on employees from different functional disciplines worldwide … regardless of region or country according to need": para. 203.
- "R&D was organized around a particular project, not particular geographical locations or legal entities, and was managed on a global basis": para. 202.
- "The fact that Nortel ensured that legal entities were properly created and advised in the various countries in

which it operated in order to meet local legal requirements [did] not mean that Nortel operated a separate business in each country. It did not”: para. 202.

- “The intangible assets that were sold, being by far the largest type of asset sold, were not separately located in any one jurisdiction or owned separately in different jurisdictions”: para. 202.
- The assets are “so intertwined that it is difficult to separate them for purposes of dealing with different entities”: para. 222.
- There is “no recognized measurable right in any one of the selling Debtor Estates to all or a fixed portion of the proceeds of sale”: para 224.
- “Nortel has had significant difficulty in determining the ownership of its princip[al] assets, namely the $7.3 billion representing the proceeds of the sales of the lines of business and the residual patent portfolio”, which “constitutes more than 80 per cent of the total assets of all Nortel entities”: para. 222.

[44] In addition to his factual findings supporting the *pro rata* order, the trial judge explained why the allocation in this case did not constitute substantive consolidation, either actual or deemed:

- The Lockbox Funds were largely due to the sale of IP and no one Debtor Estate had any right to the funds. They did not belong in whole or in part to any one Estate or combination of Estates.
- The various entities and the various Estates were not being treated as one entity and the creditors of each entity would not become creditors of a single entity. Each entity remained separate and with its own creditors.
- Each entity would maintain its own cash on hand and would be administered separately.

- The inter-company claims would not be eliminated.

[45] Similarly, Judge Gross explained at p. 554 of his reasons that the *pro rata* allocation, which was not a distribution, "both recognizes the integrity of the corporate separateness and the integrated synergistic operations of Nortel." Furthermore, he noted that a "pro rata allocation does not merge the Nortel Debtors into a single survivor and does not erase intercompany claims": p. 554.

[46] In our view, there is no *prima facie* merit to the argument that we should interfere with the trial judge's conclusion that the allocation decision did not amount to substantive consolidation. His conclusion was based on the nature and effect of his allocation decision and his factual findings. He made the findings having heard from 36 witnesses and having received and reviewed thousands of exhibits and dozens of deposition transcripts over the course of a six-week trial. Those factual findings were central to the result. Absent palpable and overriding error, those factual findings are afforded deference by this court: *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235, at para. 10.

[47] The moving parties also allege that the trial judge erred by applying an inappropriately low threshold for the application of substantive consolidation in finding that, even if the allocation did constitute substantive consolidation, it was permissible. They point to *Northland* as the leading authority on substantive consolidation but say that it is time to revisit that decision in Canada.

[48] The trial judge correctly observed that while the *CCAA* does not expressly address the issue of substantive consolidation, jurisprudence in Canada has recognized substantive consolidation as being appropriate in certain exceptional circumstances: see, for e.g., *Re Lehndorff General Partner Ltd.*, *Re PSINet Ltd.*, and *Re Northland Properties Ltd.*

[49] He also correctly observed that the court has jurisdiction to make any order that it considers appropriate in the circumstances under s. 11 of the *CCAA*. Although that section came into effect after the Nortel filing under the *CCAA*, it reflects past jurisprudence: *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60**,** [2010] 3 S.C.R. 379, at para. 68. Specifically, s. 11 states:

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

[50] That said, since there is no *prima facie* merit to the argument that the *pro rata* allocation constitutes substantive consolidation, there is no need to re-visit the jurisprudence governing substantive consolidation in Canada or to consider whether the threshold for substantive consolidation should be changed.

[51] Furthermore, we see no merit in the argument raised by the Bank of New York Mellon that the trial judge erred by failing to allocate the Lockbox Funds in a

manner consistent with the *BIA* scheme, which contemplates distribution on an entity-by-entity basis. Under the *CCAA* allocation decision, distribution to creditors will be done on an entity-by-entity basis.

[52] Finally, the argument raised by the Ad Hoc Group of Bondholders and the Official Committee also lacks merit. It presumes that the various Nortel companies had distinct and separable property rights in Nortel's IP. The trial judge repeatedly rejected that proposition. As we explain in the following sections, we see no merit in the argument that the trial judge erred in failing to recognize such distinct property rights. As such, we see no merit in the argument that he exercised his authority in a way that ignored such rights.

[53] This ground of appeal is not *prima facie* meritorious.

(ii) The Interpretation of the MRDA

Position of Moving Parties

[54] The moving parties take the position that the trial judge erred in concluding that the MRDA has no application to the allocation of the Lockbox Funds. On their reading, the MRDA provides NNI and other "Integrated Entities" with valuable rights to Nortel's IP in their respective exclusive jurisdictions. They note that the trial judge and Judge Gross diverged on the issue of IP rights under the MRDA.

[55] The thrust of their contractual argument is two-fold: (1) the trial judge misinterpreted the MRDA by disregarding the words of the agreement; and (2) he failed to apply the Supreme Court of Canada's decision in *Sattva* by taking an impermissibly narrow view of the scope of factual matrix evidence. In particular, they submit that the trial judge failed to take into account evidence relating to, and explaining, the tax-driven nature of the MRDA and the purposes the parties were trying to achieve through the agreement.

Analysis

[56] We reject the moving parties' submissions on the interpretation of the MRDA.

[57] On August 1, 2014, the Supreme Court of Canada released *Sattva*. The essence of that decision is best captured by excerpts from the reasons of the court written by Rothstein J.:

- "Historically, determining the legal rights and obligations of the parties under a written contract was considered a question of law": para. 43.

- "[T]he historical approach should be abandoned. Contractual interpretation involves issues of mixed fact and law as it is an exercise in which the principles of contractual interpretation are applied to the words of the written contract, considered in light of the factual matrix": para. 50.

- "[T]his Court in *Housen* [*v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235] found that deference to fact-finders promoted the goals of limiting the number,

> length, and cost of appeals, and of promoting the autonomy and integrity of trial proceedings …. These principles also weigh in favour of deference to first instance decision-makers on points of contractual interpretation. The legal obligations arising from a contract are, in most cases, limited to the interest of the particular parties. Given that our legal system leaves broad scope to tribunals of first instance to resolve issues of limited application, this supports treating contractual interpretation as a question of mixed fact and law": para. 52.

- "[I]t may be possible to identify an extricable question of law from within what was initially characterized as a question of mixed fact and law …. Legal errors made in the course of contractual interpretation include 'the application of an incorrect principle, the failure to consider a required element of a legal test, or the failure to consider a relevant factor'": para. 53.

- "However, courts should be cautious in identifying extricable questions of law in disputes over contractual interpretation": para. 54.

- "The close relationship between the selection and application of principles of contractual interpretation and the construction ultimately given to the instrument means that the circumstances in which a question of law can be extricated from the interpretation process will be rare": para. 55.

[58] Justice Rothstein also discussed the need to consider the surrounding circumstances, or factual matrix of a contract, when interpreting a written agreement. The goal of contractual interpretation is to ascertain the objective intentions of the parties. In doing so, "a decision-maker must read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of

formation of the contract": para. 47. Recognizing that words do not have an immutable meaning, the court should consider the contract's commercial purpose, taking into account its genesis, background, context, and the market in which the parties are operating.

[59] In this case, the moving parties suggest that the trial judge erred in his interpretation of the MRDA and failed to pay heed to *Sattva*. In our view, the moving parties' arguments are not *prima facie* meritorious.

[60] We are not persuaded that there is any reason to interfere with the trial judge's interpretation of the agreement on the basis of palpable and overriding error. Nor, in our view, have the moving parties pointed to any extricable legal error warranting intervention by this court.

[61] As mentioned, although *Sattva* was released during the course of the allocation trial, the trial judge nonetheless considered and applied *Sattva* in interpreting the MRDA. In over 40 paragraphs, he addressed the relevant law on, and evidence of, factual matrix: see paras. 55 – 57, 117 – 157. He properly rejected evidence of subjective intention as being inadmissible.

[62] We would also observe that, as noted by the Monitor and the Canadian Debtors, to be fully successful on their appeal, the U.S. Debtors would have to persuade the court that the trial judge should have: (i) concluded that the MRDA controlled allocation of Nortel's assets in the event of insolvency; (ii) adopted the

interpretation of the MRDA advanced by the U.S. Debtors; and (iii) accepted the expert valuation evidence tendered by the U.S. Debtors.

[63] The trial judge did none of these things. All of his conclusions to the contrary engage questions of fact or mixed fact and law that are well within his province.

[64] For instance, the trial judge rejected the U.S. Debtors' valuation evidence as unreliable and the moving parties' factums are silent on how this finding could be overcome. The acceptance or rejection of the evidence of a witness is squarely within the fact-finding arena of the trial judge. The moving parties have suggested no reason why the trial judge's findings on valuation would be reversed.

[65] In conclusion, this ground of appeal does not warrant granting leave to appeal.

(iii) Fairness to the Parties and Related Arguments

Position of Moving Parties

[66] Next, the moving parties submit that they were denied procedural fairness in various respects and that the allocation decision is, among other things, arbitrary, and inequitable. In this regard, we do not propose to address every argument in the multitude of factums filed. The principal submissions on fairness and related arguments that merit comment are as follows.

[67] The moving parties say they were given no notice or opportunity to make submissions on the remedy granted. Moreover, there was no record before the court on the full spectrum of claims asserted against the Selling Debtors and no one proposed the specific remedy granted.

[68] The U.S. Debtors also submit that the remedy did not respond to the question before the court, which they say was the allocation of the Sale Proceeds (i.e. the proceeds from a particular Sale Transaction) among the Selling Debtors (i.e. the Nortel parties to a particular Sale Transaction). In their view, the trial judge did not answer that question but instead allocated the Sale Proceeds to Nortel entities that did not transfer assets in a particular Sale Transaction and were, thus, not entitled to any Sale Proceeds.

[69] The Ad Hoc Group of Bondholders similarly submits that the trial judge answered the wrong question. For instance, it says that the only question properly before the court was to determine the relative value of the assets, rights and interests that each Selling Debtor sold or relinquished, which generated the Sale Proceeds. Moreover, they say that the decision disregards their legitimate expectations.

[70] The U.S. Debtors further submit that the allocation is arbitrary since there is no logical connection between what will be or will not be counted for allocation purposes. In particular, they point to the fact the allocation excludes $4 billion in

bondholder guarantee claims from the U.S. Debtors' allocation. They say that, as a result, the U.S. Debtors will receive no allocation of funds on account of approximately two-thirds of their claims.

[71] Similarly, the Ad Hoc Group of Bondholders submits the allocation is arbitrary as it produces a redistribution of assets among debtors that violates the rule that equity holders get paid after creditors.

[72] The Conflicts Administrator of NNSA also takes issue with the fairness of the allocation decision. It says that NNSA is prejudiced by the decision because of the relatively small quantum of its creditors' claims in comparison with those of other debtor estates.

[73] Finally, the Official Committee, which represents all general unsecured creditors of the U.S. Debtors, complains that the trial judge exercised his discretion in an unprincipled way and strayed into improper "commercial judicial moralism".

Analysis

[74] We are not satisfied that there is *prima facie* merit to the moving parties' submissions.

[75] As explained, the trial judge was required to "determine the allocation of the Sale Proceeds among the Selling Debtors" under the Allocation Protocol.

[76] Given the trial judge's conclusion that the MRDA did not govern allocation and his rejection of the EMEA Debtors' joint ownership theory, the trial judge had to determine what other metric should be used to allocate the Lockbox Funds among the U.S., Canadian and EMEA Debtor Estates.

[77] The Allocation Protocol permitted submissions on "any theory of allocation". At trial, the UKPC and the CCC, in the alternative, sought a *pro rata* distribution of the funds held in escrow and each submitted expert reports that supported a *pro rata* result. Moreover, the U.S. Debtors, the Official Committee and the Ad Hoc Group of Bondholders all made submissions before the trial judge opposing a *pro rata* allocation and had an opportunity to test the evidence. They submitted a motion to strike the *pro rata* allocation evidence, attacked the reliability of the expert reports and cross-examined the experts.

[78] Thus, all parties knew that a *pro rata* allocation was in play. The fact that the specifics of the allocation ordered by the trial judge were not identical to those advanced by any of the parties does not, in our view, create unfairness to the parties. This is not a situation where the trial judge addressed an issue that was not before him, failed to grapple with the arguments or evidence, or came up with a new theory of the case.

[79] The two judges were not required to determine value but allocation. The IFSA provided for a right to receive an allocation of the Sale Proceeds without

restricting the basis upon which that allocation might be determined by the two courts. In particular, we note that the trial judges were given authority to decide the issue of allocation. In addition to the terms of the Allocation Protocol, we note s.10(a) of the IFSA:

> [T]his Agreement is not, and shall not be deemed to be, an acknowledgement by any Party of the assumption, ratification, adoption or rejection of the Transfer Pricing Agreements or any other Transfer Pricing methodology employed by the Nortel Group or its individual members for any purpose nor shall it be determinative of, or have any impact whatsoever on, the allocation of proceeds to any Debtor from any sale of assets of the Nortel Group; [Emphasis added.]

[80] We also observe that the trial judge turned his mind to expectations and found that there was no evidence to support the Bondholders' argument that their legitimate expectations would be disregarded by a *pro rata* allocation.

[81] Furthermore, we see no basis for the assertion that the allocation framework is arbitrary and unfair since it excludes $4 billion in Bondholder guarantee claims from the U.S. Debtors' allocation. Under the allocation decision, a claim that can be made against more than one Debtor Estate can only be calculated and recognized once for allocation purposes. This principle is applicable to all claims. The allocation decision also specifies that claims on bonds are to be made on the Debtor Estate of the issuer. Claims on those bonds may also be made on the Debtor Estate of the guarantor but those claims will not

be taken into account in determining the claims against the Debtor Estates for allocation purposes.

[82] On the reconsideration motion, it was argued that the trial judge's decision should be changed to provide that the claims by the bondholders on the guaranteed bonds against the issuer and guarantor Debtor Estates should be included in the claims for allocation purposes. It was contended that, without such a change, there would be a manifest injustice, especially to the creditors of the U.S. Debtors other than the bondholders.

[83] The trial judge rejected that argument, noting that the $2 billion admitted claim against NNL endures. Further, cash on hand in the U.S. Debtors' Estates would be available to their creditors. He also noted that the issue of the treatment of the guaranteed bonds, and whether they should be counted once or twice in a *pro rata* allocation, was a live issue in evidence at trial, which was open to the U.S. Debtors to explore. He found, at para. 16, that "any lack of briefing by the U.S. Debtors and the [Official Committee] was a deliberate tactic taken by them in attacking the pro rata allocation method proposed at trial". He concluded that, even if he were to reconsider the double-counting issue, he would not change his mind:

> I see no injustice in the result…. There must also be considered other claims that could be made against more than one Debtor Estate, including the pension claim by the UKPC against NNUK that could be made

> against other EMEA Debtors and claims that could be made on bonds issued by NNL and guaranteed by NNC. The allocation decision precludes the double counting of any such claims for allocation purposes. The U.S. Debtors and [Official Committee] do not suggest that any of these other claims should be permitted to be claimed twice for allocation purposes. I see no basis to treat the guaranteed bonds any differently for allocation purposes. The principles that govern allocation should be applied consistently to each debtor.

[84] We are not persuaded that there is *prima facie* merit to the argument that the allocation is arbitrary. The trial judge was clearly alive to the fairness concerns and gave reasons for adopting the approach he did after careful consideration of the evidence and argument at trial.

[85] We would also observe that there was no other clear answer to the question of who was entitled to receive the sale proceeds. As Judge Gross noted at p. 500 of his reasons, the parties "submitted widely varying approaches for deciding the issue leaving virtually no middle ground." The U.S. Debtors and Bondholders argued that in excess of $5 billion belonged to the U.S. Estate and that the Canadian Estate should receive only $0.77 billion. The Canadian Debtors and the Monitor, in sharp contrast, argued that in excess of $6 billion belonged to the Canadian Estate and that the U.S. Estate should receive just over $1 billion. The highly integrated nature of the Nortel business operations and the nature of the assets sold defied either outcome.

[86] Judge Gross's comments in his reasons on the allocation trial, at pp. 532-533, accurately sum up the context in which the two courts came to adopt the *pro rata* allocation approach:

> The Court is convinced that where, as here, operating entities in an integrated, multi-national enterprise developed assets in common and there is nothing in the law or facts giving any of those entities certain and calculable claims to the proceeds from the liquidation of those assets in an enterprise-wide insolvency, adopting a pro rata allocation approach, which recognizes inter-company and settlement related claims and cash in hand, yields the most acceptable result.
>
> There is nothing in the law or facts of this case which weighs in favour of adopting one of the wide ranging approaches of the Debtors. There is no uniform code or international treaty or binding agreement which governs how Nortel is to allocate the Sales Proceeds between the various insolvency estates or subsidiaries spread across the globe.

[87] Nor are we satisfied that there is *prima facie* merit to the Official Committee's argument that the trial judge exercised his discretion in an unprincipled way by straying into improper "commercial judicial moralism". To the extent the Official Committee is suggesting that it amounts to judicial moralism when a judge takes into account fairness concerns, we reject that argument. The trial judge considered the evidence before him in considerable detail and worked with the facts presented to him. Based on those facts, he concluded that a *pro rata* order constituted the answer to the allocation issue. The fact that the answer is also fair should not detract from the force of his conclusion.

[88] Finally, we are not persuaded that there is any merit to the argument that the allocation violates the rule that equity holders get paid after creditors. The Ad Hoc Group of Bondholders submits that the trial judge's decision results in NNL (NNI's parent company) receiving allocation proceeds from the sale of NNI's assets and rights that ought to have been allocated to the NNI estate for the benefit of NNI's creditors. This argument is premised on NNI having a right to the particular proceeds as a result of the MRDA interpretation advanced by the U.S. Debtors and Bondholders. As we have discussed above, the trial judge rejected that argument.

[89] For these reasons, we conclude that none of the fairness and related arguments put forward by the moving parties are *prima facie* meritorious.

(b) Significance of Issues to the Practice

Position of Moving Parties

[90] The moving parties submit that the trial judge's decision presents important issues of first impression in the cross-border insolvency context. They submit that, without appellate intervention, there is a risk substantive consolidation will become far more widely available. In addition, they say that it creates significant uncertainty on the separation of subsidiaries within a corporate group and on the consequences of an insolvency proceeding on the rights of stakeholders, including creditors. In their submission, an appeal would permit this court to

clarify these issues. Furthermore, the appeal would allow this court to clarify the proper interpretation and effect of *Sattva* on commercial agreements.

Analysis

[91] As discussed above, the moving parties have raised three main issues they say warrant leave – namely, substantive consolidation, the interpretation of the MRDA, and fairness. Of the three issues, the moving parties submit that the first two raise issues of significant interest to the practice.

[92] We disagree.

[93] The facts of this case are unique and exceptional. As we have already discussed, substantive consolidation is not engaged and so this case would not provide an opportunity for this court to provide guidance on that question. Nor does this case engage any issues that require any clarification on the application of *Sattva*. In short, granting leave would not provide an opportunity for this court to provide guidance on legal issues of significance to the practice.

(c) Significance of Issues to the Action

Position of Moving Parties

[94] The moving parties state that the allocation of the Lockbox Funds is the overriding issue in the *CCAA* proceedings.

Analysis

[95] We accept that the allocation of the Lockbox Funds is a significant issue in this *CCAA* proceeding. That said, we are of the view that, standing alone, this factor is insufficient to warrant granting leave to appeal. To perhaps state the obvious, typically parties tend to seek leave to appeal a decision that is of significance to an action.

(d) Progress of Proceedings

Position of Moving Parties

[96] The moving parties submit that the proposed appeal will not unduly hinder the progress of Nortel's *CCAA* proceeding. They state that many steps and issues remain before creditor distributions can be made, including the determination of claims. In addition, the allocation decisions of the Canadian court and the U.S. court must both be final orders in their respective jurisdictions before funds can be released from escrow. It is argued that this court should grant leave to ensure that it maintains the ability to address any issues should Judge Gross's decision be varied or overturned on appeal.

[97] The moving parties also make the point that there are no operating businesses that are in the process of restructuring because the Nortel businesses and assets have been liquidated and the joint trial was a "stand-alone component" of the *CCAA* proceeding. Thus, it is argued that the traditional

concerns leading courts to “sparingly” grant leave to appeal in *CCAA* proceedings are not applicable here. In fact, the Official Committee submits that where an appeal would have existed as of right under the *BIA*, it is nonsensical to deny leave here simply because Nortel’s liquidation proceeded under the *CCAA*.

Analysis

[98] This brings us to the final consideration: progress. Repeatedly, the parties have been encouraged to resolve their differences, but without success. For instance, in a 2011 decision, *In re Nortel Networks, Inc.*, 669 F.3d 128, the Third Circuit Court of Appeals admonished the parties at p. 143:

> We are concerned that the attorneys representing the respective sparring parties may be focusing on some of the technical differences governing bankruptcy in the various jurisdictions without considering that there are real live individuals who will ultimately be affected by the decisions being made in the courtrooms. It appears that the largest claimants are pension funds in the U.K. and the United States, representing pensioners who are undoubtedly dependent, or who will become dependent, on their pensions. They are the Pawns in the moves being made by the Knights and the Rooks.
>
> Mediation, or continuation of whatever mediation is ongoing, by the parties in good faith is needed to resolve the differences. [Footnote omitted.]

[99] Former Chief Justice Winkler also encouraged the parties to find a way to resolve this matter. In April 2012, he warned about the “prospect of additional delays and the potential for conflicting decisions” if the parties failed to reach a negotiated settlement.

[100] Numerous mediations have been ordered but have failed.

[101] In the Annual Review of Insolvency, Kevin P. McElcheran described *Nortel* as a case that has become "an emblem of waste and dysfunction in a system intended to foster consensus based solutions to commercial insolvency", noting that it has "eclipsed all previous Canadian cases in both duration and expense": 2014 Ann. Rev. Insolv. L. 24 at p. 24. And that was in 2014.

[102] Consistent allocation decisions have been issued by the Canadian and U.S. courts. A further appeal proceeding in Canada would achieve nothing but more delay, greater expense, and an erosion of creditor recoveries. There are asymmetric appeal routes in Canada and the U.S. However, we do not accept that the separate appeal proceedings in the U.S. somehow diminish the need to bring these proceedings in Canada to a conclusion. In our view, any additional step is a barrier to progress.

[103] Furthermore, the fact that this case is a liquidation and not a restructuring does not render delay immaterial, where so many individuals and businesses continue to await a resolution of this proceeding. The potential of an interim distribution, remote or otherwise, does not alter this reality. In addition, the parties acceded to a liquidation under the *CCAA*. They cannot now reject the parameters of that statute, which requires leave to appeal, and where the jurisprudence on the applicable test is settled and long-standing.

E. STANDING ISSUE

[104] There is the additional issue of the standing of the Nortel Trade Claims Consortium that needs to be addressed. It represents a group of creditors that collectively holds over $130 million in unsecured claims against NNI and certain of its U.S. affiliates. It includes institutional investors and former Nortel employees. Unlike other U.S. creditors, the Consortium's sole recourse is against the U.S. Debtors' estates.

[105] At trial, the Consortium was represented by the Official Committee. It says that, given the trial decision, its interests may diverge from those of the rest of the Official Committee. It submits that the Consortium should have standing to seek leave to appeal. It relies on the court's jurisdiction to grant leave to appeal, pursuant to s. 13 of the *CCAA*, to "any person dissatisfied with an order or a decision made under [the] Act". It argues that the trial judge exceeded his jurisdiction by deciding matters that are properly for the U.S. court to decide.

[106] It is unnecessary to decide the standing issue. Even if the Consortium had standing, we would dismiss its leave motion for the same reasons we have dismissed the other leave motions. In any event, we see no merit in its argument that the trial judge exceeded his jurisdiction.

F. DISPOSITION

[107] In conclusion, we are not persuaded that the test for leave to appeal has been met. For these reasons, we dismiss all of the motions for leave to appeal.

Released:

“AH”	“Alexandra Hoy A.C.J.O.”
“MAY -3 2016”	“R.A. Blair J.A.”
	“S.E. Pepall J.A.”

TAB 3

CITATION: Canwest Publishing Inc., 2010 ONSC 1328
COURT FILE NO.: CV-10-8533-00CL
DATE: 20100305

ONTARIO

SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

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

AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT OF CANWEST PUBLISHING INC./PUBLICATIONS CANWEST INC., CANWEST BOOKS INC. AND CANWEST (CANADA) INC.

COUNSEL: *Lyndon Barnes and Alex Cobb* for the Canwest LP Entities
Maria Konyukhova for the Monitor, FTI Consulting Canada Inc.
Hilary Clarke for the Bank of Nova Scotia, Administrative Agent for the Senior Secured Lenders' Syndicate
Janice Payne and Thomas McRae for the Canwest Salaried Employees and Retirees (CSER) Group
M. A. Church for the Communications, Energy and Paperworkers' Union
Anthony F. Dale for CAW-Canada
Deborah McPhail for the Financial Services Commission of Ontario

PEPALL J.

REASONS FOR DECISION

Relief Requested

[1] Russell Mills, Blair MacKenzie, Rejean Saumure and Les Bale (the "Representatives") seek to be appointed as representatives on behalf of former salaried employees and retirees of Canwest Publishing Inc./Publications Canwest Inc., Canwest Books Inc., Canwest (Canada) and Canwest Limited Partnership and the Canwest Global Canadian Newspaper Entities (collectively the "LP Entities") or any person claiming an interest under or on behalf of such salaried

employees or retirees including beneficiaries and surviving spouses ("the Salaried Employees and Retirees"). They also seek an order that Nelligan O'Brien Payne LLP and Shibley Righton LLP be appointed in these proceedings to represent the Salaried Employees and Retirees for all matters relating to claims against the LP Entities and any issues affecting them in the proceedings. Amongst other things, it is proposed that all reasonable legal, actuarial and financial expert and advisory fees be paid by the LP Entities.

[2] On February 22, 2010, I granted an order on consent of the LP Entities authorizing the Communications, Energy and Paperworker's Union of Canada ("CEP") to continue to represent its current members and to represent former members of bargaining units represented by the union including pensioners, retirees, deferred vested participants and surviving spouses and dependants employed or formerly employed by the LP Entities. That order only extended to unionized members or former members. The within motion focused on non-unionized former employees and retirees although Ms. Payne for the moving parties indicated that the moving parties would be content to include other non-unionized employees as well. There is no overlap between the order granted to CEP and the order requested by the Salaried Employees and Retirees.

<u>Facts</u>

[3] On January 8, 2010 the LP Entities obtained an order pursuant to the *Companies' Creditors Arrangement Act* ("CCAA") staying all proceedings and claims against the LP Entities. The order permits but does not require the LP Entities to make payments to employee and retirement benefit plans.

[4] There are approximately 66 employees, 45 of whom were non-unionized, whose employment with the LP Entities terminated prior to the Initial Order but who were still owed termination and severance payments. As of the date of the Initial Order, the LP Entities ceased making those payments to those former employees. As many of these former employees were owed termination payments as part of a salary continuance scheme whereby they would continue to accrue pensionable service during a notice period, after the Initial Order, those former

employees stopped accruing pensionable service. The Representatives seek an order authorizing them to act for the 45 individuals and for the aforementioned law firms to be appointed as representative counsel.

[5] Additionally, seven retirees and two current employees are (or would be) eligible for a pension benefit from Southam Executive Retirement Arrangements ("SERA"). SERA is a non-registered pension plan used to provide supplemental pension benefits to former executives of the LP Entities and their predecessors. These benefits are in excess of those earned under the Canwest Southam Publications Inc. Retirement Plan which benefits are capped as a result of certain provisions of the *Income Tax Act*. As of the date of the Initial Order, the SERA payments ceased also. This impacts beneficiaries and spouses who are eligible for a joint survivorship option. The aggregate benefit obligation related to SERA is approximately $14.4 million. The Representatives also seek to act for these seven retirees and for the aforementioned law firms to be appointed as representative counsel.

[6] Since January 8, 2010, the LP Entities have being pursuing the sale and investor solicitation process ("SISP") contemplated by the Initial Order. Throughout the course of the CCAA proceedings, the LP Entities have continued to pay:

(a) salaries, commissions, bonuses and outstanding employee expenses;

(b) current services and special payments in respect of the active registered pension plan; and

(c) post-employment and post-retirement benefits to former employees who were represented by a union when they were employed by the LP Entities.

[7] The LP Entities intend to continue to pay these employee related obligations throughout the course of the CCAA proceedings. Pursuant to the Support Agreement with the LP Secured Lenders, AcquireCo. will assume all of the employee related obligations including existing pension plans (other than supplemental pension plans such as SERA), existing post-retirement and post-employment benefit plans and unpaid severance obligations stayed during the CCAA

proceeding. This assumption by AcquireCo. is subject to the LP Secured Lenders' right, acting commercially reasonably and after consultation with the operational management of the LP Entities, to exclude certain specified liabilities.

[8] All four proposed Representatives have claims against the LP Entities that are representative of the claims that would be advanced by former employees, namely pension benefits and compensation for involuntary terminations. In addition to the claims against the LP Entities, the proposed Representatives may have claims against the directors of the LP Entities that are currently impacted by the CCAA proceedings.

[9] No issue is taken with the proposed Representatives nor with the experience and competence of the proposed law firms, namely Nelligan O'Brien Payne LLP and Shibley Righton LLP, both of whom have jointly acted as court appointed representatives for continuing employees in the Nortel Networks Limited case.

[10] Funding by the LP Entities in respect of the representation requested would violate the Support Agreement dated January 8, 2010 between the LP Entities and the LP Administrative Agent. Specifically, section 5.1(j) of the Support Agreement states:

> "The LP Entities shall not pay any of the legal, financial or other advisors to any other Person, except as expressly contemplated by the Initial Order or with the consent in writing from the Administrative Agent acting in consultation with the Steering Committee."

[11] The LP Administrative Agent does not consent to the funding request at this time.

[12] On October 6, 2009, the CMI Entities applied for protection pursuant to the provisions of the CCAA. In that restructuring, the CMI Entities themselves moved to appoint and fund a law firm as representative counsel for former employees and retirees. That order was granted.

[13] Counsel were urged by me to ascertain whether there was any possibility of resolving this issue. Some time was spent attempting to do so, however, I was subsequently advised that those efforts were unsuccessful.

Issues

[14] The issues on this motion are as follows:

(1) Should the Representatives be appointed?

(2) Should Nelligan O'Brien Payne LLP and Shibley Righton LLP be appointed as representative counsel?

(3) If so, should the request for funding be granted?

Positions of Parties

[15] In brief, the moving parties submit that representative counsel should be appointed where vulnerable creditors have little means to pursue a claim in a complex CCAA proceeding; there is a social benefit to be derived from assisting vulnerable creditors; and a benefit would be provided to the overall CCAA process by introducing efficiency for all parties involved. The moving parties submit that all of these principles have been met in this case.

[16] The LP Entities oppose the relief requested on the grounds that it is premature. The amounts outstanding to the representative group are prefiling unsecured obligations. Unless a superior offer is received in the SISP that is currently underway, the LP Entities will implement a support transaction with the LP Secured Lenders that does not contemplate any recoveries for unsecured creditors. As such, there is no current need to carry out a claims process. Although a superior offer may materialize in the SISP, the outcome of the SISP is currently unknown.

[17] Furthermore, the LP Entities oppose the funding request. The fees will deplete the resources of the Estate without any possible corresponding benefit and the Support Agreement with the LP Secured Lenders does not authorize any such payment.

[18] The LP Senior Lenders support the position of the LP Entities.

[19] In its third report, the Monitor noted that pursuant to the Support Agreement, the LP Entities are not permitted to pay any of the legal, financial or other advisors absent consent in writing from the LP Administrative Agent which has not been forthcoming. Accordingly, funding of the fees requested would be in contravention of the Support Agreement with the LP Secured Lenders. For those reasons, the Monitor supported the LP Entities refusal to fund.

Discussion

[20] No one challenged the court's jurisdiction to make a representation order and such orders have been granted in large CCAA proceedings. Examples include Nortel Networks Corp., Fraser Papers Inc., and Canwest Global Communications Corp. (with respect to the television side of the enterprise). Indeed, a human resources manager at the Ottawa Citizen advised one of the Representatives, Mr. Saumure, that as part of the CCAA process, it was normal practice for the court to appoint a law firm to represent former employees as a group.

[21] Factors that have been considered by courts in granting these orders include:

- the vulnerability and resources of the group sought to be represented;

- any benefit to the companies under CCAA protection;

- any social benefit to be derived from representation of the group;

- the facilitation of the administration of the proceedings and efficiency;

- the avoidance of a multiplicity of legal retainers;

- the balance of convenience and whether it is fair and just including to the creditors of the Estate;

- whether representative counsel has already been appointed for those who have similar interests to the group seeking representation and who is also prepared to act for the group seeking the order; and

- the position of other stakeholders and the Monitor.

[22] The evidence before me consists of affidavits from three of the four proposed Representatives and a partner with the Nelligan O'Brien Payne LLP law firm, the Monitor's Third Report, and a compendium containing an affidavit of an investment manager for noteholders filed on an earlier occasion in these CCAA proceedings. This evidence addresses most of the aforementioned factors.

[23] The primary objection to the relief requested is prematurity. This is reflected in correspondence sent by counsel for the LP Entities to counsel for the Senior Lenders' Administrative Agent. Those opposing the relief requested submit that the moving parties can keep an eye on the Monitor's website and depend on notice to be given by the Monitor in the event that unsecured creditors have any entitlement. Counsel for the LP Entities submitted that counsel for the proposed representatives should reapply to court at the appropriate time and that I should dismiss the motion without prejudice to the moving parties to bring it back on.

[24] In my view, this watch and wait suggestion is unhelpful to the needs of the Salaried Employees and Retirees and to the interests of the Applicants. I accept that the individuals in issue may be unsecured creditors whose recovery expectation may prove to be non-existent and that ultimately there may be no claims process for them. I also accept that some of them were in the executive ranks of the LP Entities and continue to benefit from payment of some pension benefits. That said, these are all individuals who find themselves in uncertain times facing legal proceedings of significant complexity. The evidence is also to the effect that members of the group have little means to pursue representation and are unable to afford proper legal representation at this time. The Monitor already has very extensive responsibilities as reflected in paragraph 30 and following of the Initial Order and the CCAA itself and it is unrealistic to expect that it can be fully responsive to the needs and demands of all of these many individuals and do so in an efficient and timely manner. Desirably in my view, Canadian courts have not typically appointed an Unsecured Creditors Committee to address the needs of unsecured creditors in large restructurings. It would be of considerable benefit to both the Applicants and

the Salaried Employees and Retirees to have Representatives and representative counsel who could interact with the Applicants and represent the interests of the Salaried Employees and Retirees. In that regard, I accept their evidence that they are a vulnerable group and there is no other counsel available to represent their interests. Furthermore, a multiplicity of legal retainers is to be discouraged. In my view, it is a false economy to watch and wait. Indeed the time taken by counsel preparing for and arguing this motion is just one such example. The appointment of the Representatives and representative counsel would facilitate the administration of the proceedings and information flow and provide for efficiency.

[25] The second basis for objection is that the LP Entities are not permitted to pay any of the legal, financial or other advisors to any other person except as expressly contemplated by the Initial Order or with consent in writing from the LP Administrative Agent acting in consultation with the Steering Committee. Funding by the LP Entities would be in contravention of the Support Agreement entered into by the LP Entities and the LP Senior Secured Lenders. It was for this reason that the Monitor stated in its Report that it supported the LP Entities' refusal to fund.

[26] I accept the evidence before me on the inability of the Salaried Employees and Retirees to afford legal counsel at this time. There are in these circumstances three possible sources of funding: the LP Entities; the Monitor pursuant to paragraph 31 (i) of the Initial Order although quere whether this is in keeping with the intention underlying that provision; or the LP Senior Secured Lenders. It seems to me that having exercised the degree of control that they have, it is certainly arguable that relying on inherent jurisdiction, the court has the power to compel the Senior Secured Lenders to fund or alternatively compel the LP Administrative Agent to consent to funding. By executing agreements such as the Support Agreement, parties cannot oust the jurisdiction of the court.

[27] In my view, a source of funding other than the Salaried Employees and Retirees themselves should be identified now. In the CMI Entities' CCAA proceeding, funding was made available for Representative Counsel although I acknowledge that the circumstances here

are somewhat different. Staged payments commencing with the sum of $25,000 may be more appropriate. Funding would be prospective in nature and would not extend to investigation of or claims against directors.

[28] Counsel are to communicate with one another to ascertain how best to structure the funding and report to me if necessary at a 9:30 appointment on March 22, 2010. If everything is resolved, only the Monitor need report at that time and may do so by e-mail. If not resolved, I propose to make the structuring order on March 22, 2010 on a nunc pro tunc basis. Ottawa counsel may participate by telephone but should alert the Commercial List Office of their proposed mode of participation.

Pepall J.

Released: March 5, 2010

CITATION: Canwest Publishing Inc., 2010 ONSC 1328
COURT FILE NO.: CV-10-8533-00CL
DATE: 20100305

ONTARIO

SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

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

AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT OF CANWEST PUBLISHING INC./ PUBLICATIONS CANWEST INC., CANWEST BOOKS INC., AND CANWEST (CANADA) INC.

REASONS FOR DECISION

Pepall J.

Released: March 5, 2010

TAB 4

COURT OF APPEAL FOR ONTARIO

CITATION: Laurentian University of Sudbury (Re), 2021 ONCA 199
DATE: 20210331
DOCKET: M52287

Hoy, Pepall and Zarnett JJ.A.

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 Laurentian University of Sudbury

Murray Gold and James Harnum, for the moving party the Ontario Confederation of University Faculty Associations

Susan Philpott and Charles Sinclair, for the moving party the Laurentian University Faculty Association

Miriam Martin, for the moving party the Canadian Union of Public Employees

D.J. Miller, Scott McGrath and Derek Harland, for the responding party Laurentian University of Sudbury

Ashley Taylor, Elizabeth Pillon and Zev Smith, for the responding party Ernst & Young Inc., acting as the Monitor

Heard: in writing

Motion for leave to appeal from the order of Chief Justice Geoffrey B. Morawetz of the Superior Court of Justice, dated February 26, 2021.

REASONS FOR DECISION

[1] Laurentian University of Sudbury ("Laurentian") is a publicly funded, bilingual and tricultural post-secondary institution, serving domestic and international undergraduate and graduate students. Due to recurring operational deficits, it has encountered a liquidity crisis and is insolvent.

[2] Laurentian sought and obtained protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C.36 ("CCAA"), to permit it to restructure, financially and operationally, in order to emerge as a sustainable university for the benefit of all stakeholders. Among the stated reasons for Laurentian's CCAA application was what it described as unsustainable "academic costs", which Laurentian attributes in part to the terms of its collective agreement with its faculty members.

[3] Two unions representing Laurentian employees - the Laurentian University Faculty Association ("LUFA") and the Canadian Union of Public Employees ("CUPE") - and the Ontario Confederation of University Faculty Associations ("OCUFA"), an umbrella organization representing faculty associations, seek leave to appeal the decision of the CCAA judge, dated February 26, 2021, which continues a sealing order over two documents that Laurentian filed on its application for CCAA protection.

[4] Having reviewed the written submissions of the parties and the sealed documents, we refuse leave for the reasons that follow.

Background

[5] On February 1, 2021, the CCAA judge made an order (the "Initial Order"), granting Laurentian initial relief under the CCAA.

[6] Four days later, on February 5, 2021, the CCAA judge made an order appointing Dunphy J. as mediator to conduct a confidential mediation among Laurentian's key stakeholders. The mediation is intended to address various issues concerning Laurentian's restructuring, including a new collective agreement with LUFA, which represents 612 Laurentian faculty, accounting for 60% of the university's payroll. LUFA supported the appointment of the mediator.

[7] The Initial Order contained a sealing provision. At the comeback hearing, there was opposition to it. The CCAA judge continued the sealing provision in the Amended and Restated Order, dated February 11, 2021, on an interim basis, pending a supplementary endorsement.

[8] The sealing provision, which was identical in both orders, covers two exhibits (Exhibits "EEE" and "FFF") to the affidavit by Dr. Robert Haché, which was filed in support of Laurentian's request for the Initial Order. Dr. Haché is the President, Vice-Chancellor and CEO of Laurentian.

[9] The sealing provision states that the Exhibits "are herby sealed pending further order of the Court, and shall not form part of the public record". Both the

Initial Order and the Amended and Restated Order provide that any interested party may apply on seven days' notice to vary or amend the order.

[10] The sealed Exhibits consist of two letters. Exhibit "EEE" is a letter from the Ministry of Colleges and Universities ("Ministry") to Laurentian, dated January 21, 2021. Exhibit "FFF" is a letter from Laurentian to the Ministry, dated January 25, 2021. Laurentian has described the letters as containing "information with respect to [Laurentian] and certain of its stakeholders, including various rights or positions that stakeholders or [Laurentian] may take either inside or outside of these CCAA proceedings, the disclosure of which could jeopardize [Laurentian's] efforts to restructure."

[11] None of the moving parties sought to cross-examine Dr. Haché on his affidavit or the communications between Laurentian and the Ministry.

[12] The CCAA judge released his supplementary endorsement on February 26, 2021, continuing the sealing provision. The effect of the sealing provision is that both the broader public and the parties to the CCAA proceeding are prevented from accessing the Exhibits.

[13] The CCAA judge held that the sealing provision was authorized under s. 137(2) of the *Courts of Justice Act*, R.S.O. 1990, c. C.43, and by the application of the principles in *Sierra Club of Canada v. Canada (Minister of Finance)*, 2002

SCC 41, [2002] 2 S.C.R. 522. According to *Sierra Club*, at para. 53, a confidentiality or sealing order should only be granted when:

> (a) such an order is necessary in order to prevent a serious risk to an important interest, including a commercial interest, in the context of litigation because reasonably alternative measures will not prevent the risk; and
>
> (b) the salutary effects of the confidentiality order, including the effects on the right of civil litigants to a fair trial, outweigh its deleterious effects, including the effects on the right to free expression, which in this context includes the public interest in open and accessible court proceedings.

[14] The CCAA judge summarized the evidence in Dr. Haché's affidavit and noted that he had reviewed the Exhibits in detail. He indicated that the evidence, as contained in Dr. Haché's affidavit, outlines that there has been continuous communication between Laurentian and the Ministry with respect to Laurentian's financial crisis, and that the government is well aware that a real-time solution must be found if Laurentian is to survive. He noted that "the role, if any, that the Ministry will play is at this moment uncertain."

[15] Considering the first branch of the *Sierra Club* test, he concluded that disclosure of the Exhibits, "<u>at this time</u>, could be detrimental to any potential restructuring of [Laurentian]" (emphasis added). Accordingly, "the risk in disclosing the Exhibits is real and substantial and poses a serious risk to the

future viability of [Laurentian].” He also noted that “it is speculative to conclude that the Exhibits contain information that is not helpful to [Laurentian’s] position.”

[16] He found that the commercial interest was that of the entire Laurentian community, including the faculty, students, employees, third-party suppliers and the City of Greater Sudbury and the surrounding area; that it is of paramount importance to these groups that all efforts to restructure Laurentian be explored; and that it is necessary to maintain the confidentiality of the Exhibits in order to do so. He reiterated that “[t]he disclosure of the Exhibits, <u>at this time,</u> could undermine the restructuring efforts being undertaken by [Laurentian]” (emphasis added).

[17] He was not satisfied that there were any reasonable alternatives to a sealing order over the Exhibits. Stakeholders were involved in the mediation and the negotiations could or could shortly be at a sensitive stage. It would not be appropriate to implement any alternative to a confidentiality order. To do so could negatively impact the mediation efforts.

[18] Turning to the second branch of the *Sierra Club* test, the CCAA judge was also satisfied, based on the evidence, that the salutary effects of the sealing provision outweighed its deleterious effects, including the public interest in accessing the Exhibits.

Leave Test

[19] Section 13 of the CCAA provides that any person dissatisfied with an order or a decision made under the CCAA may appeal from the order or decision with leave. Leave to appeal in CCAA proceedings is to be granted sparingly and only where there are serious and arguable grounds that are of real and significant interest to the parties. This cautious approach is a function of several factors.

[20] First, a high degree of deference is owed to discretionary decisions made by judges supervising CCAA proceedings, who are "steeped in the intricacies of the *CCAA* proceedings they oversee". Appellate intervention is justified only where the "supervising judge erred in principle or exercised their discretion unreasonably": *9354-9186 Québec inc. v. Callidus Capital Corp.*, 2020 SCC 10, 78 C.B.R. (6th) 1, at paras. 53 to 54.

[21] Second, CCAA proceedings are dynamic. It is often "inappropriate to consider an exercise of discretion by the supervising judge in isolation of other exercises of discretion by the judge in endeavouring to balance the various interests": *Edgewater Casino Inc. (Re)*, 2009 BCCA 40, 51 C.B.R. (5th) 1, at para 20.

[22] Third, CCAA restructurings can be time sensitive. The existence of, and delay involved in, an appeal can be counterproductive to a successful restructuring.

[23] In addressing whether leave should be granted, the court will consider four factors, specifically whether:

(a) the proposed appeal is *prima facie* meritorious or frivolous;

(b) the points on the proposed appeal are of significance to the practice;

(c) the points on the proposed appeal are of significance to the action; and

(d) whether the proposed appeal will unduly hinder the progress of the action.

See: *Nortel Networks Corp. (Re)*, 2016 ONCA 332, 130 O.R. (3d) 481, at para. 34.

Leave is Not Warranted

[24] As we will explain, we refuse to grant leave because the proposed appeal is not *prima facie* meritorious, granting leave would unduly hinder the progress of the action, and the proposed appeal is not of significance to the action. This is not an appropriate case for this court to explore issues of significance to the practice relating to the granting of sealing orders in the CCAA context.

Leave Not *Prima Facie* Meritorious

[25] The moving parties raise three questions for determination on their proposed appeal, which we paraphrase as follows:

> 1. Did the CCAA judge err in focussing solely on Laurentian's assertion of an important commercial interest without balancing the various competing interests applicable to a sealing order?

2. Did the CCAA judge err in granting the sealing provision without a sufficient evidentiary foundation?

3. Did the CCAA judge err in concluding that the sealing provision was justified as a result of speculative concerns about the impact that disclosure of the Exhibits that were sealed would have on the CCAA restructuring process?

[26] A significant plank of the moving parties' argument is that the sealing provision denies access to the sealed documents to parties to the CCAA process on the ostensible ground that the documents might have an impact on the positions those parties choose to take vis-à-vis the restructuring. They argue that the importance of the documents to the formulation of their positions is the exact reason why they should have access to the documents, not a justification for denying access to them.

[27] We note that one of the moving parties, OCUFA, is not a creditor of Laurentian and is apparently not participating in the court-ordered mediation, the aim of which is a consensual restructuring. It is not clear in what sense OCUFA is a party to the CCAA proceeding or is in any different position than any other member of the public who may be interested in the court-filed materials. Yet the moving parties do not differentiate, in their proposed appeal questions or in the relief they propose to seek, between the entitlements of OCUFA to obtain the documents and those of the other moving parties. In other words, although reference is made to the denial of access to "litigants", the underlying theory of

the moving parties actually starts and stops with the proposition that there should be no sealing order at all.

[28] We are not persuaded that the proposed appeal, challenging what is a discretionary order, is *prima facie* meritorious.

[29] The CCAA judge set out the *Sierra Club* test in his reasons. Contrary to the submissions of the moving parties, he was well aware that *Sierra Club* required him to balance the deleterious effects of the sealing order.

[30] In earlier reasons, the CCAA judge noted that if the restructuring is to be successful, it will have to be largely completed by the end of April 2021. The timeline is exceptionally short. In exercising his discretion, the CCAA judge concluded that the risk to the potential restructuring of Laurentian within this extremely tight timeframe if the Exhibits were disclosed outweighed other relevant interests.

[31] The moving parties were (and are) concerned that they understand the Ontario government's position in relation to the restructuring, yet they did not seek to cross-examine Dr. Haché. The CCAA judge, who reviewed the Exhibits, strove to address that concern, carefully signaling that "the role, if any, that the Ministry will play is at this moment uncertain." Alive to concerns about fairness, he also signaled to the parties that it would be "speculative to conclude that the Exhibits contain information that is not helpful to [Laurentian's] position."

[32] The moving parties have expressed particular concern that the sealing order creates an informational imbalance that may hurt them in the mediation process. Nothing before us suggests that the moving parties who are participating in the court-ordered mediation (which appears to be only LUFA) have been hampered by any informational imbalance. The judicial mediator, who was appointed by the CCAA judge, is a bulwark against unfair treatment in the mediation. Should the judicial mediator have concerns that the moving parties have been hampered in the mediation by an informational imbalance or a perceived informational imbalance, it is open to him to raise them with the CCAA judge within the parameters of the February 5, 2021 order appointing the mediator.

[33] Nor do we see anything in the sealing provision that would prevent a party from making a request to the CCAA judge, at the appropriate time, for relief on appropriate terms. As noted, the sealing provision is expressly subject to "further order of the Court". The CCAA judge in his reasons of February 26 said only that an alternative to the sealing provision was not appropriate "at this time".

[34] In seeking leave, the moving parties have raised questions about how s. 2(d) of the *Charter of Rights and Freedoms* comes into play, as one of the purposes of the mediation is to conclude a new collective agreement with LUFA. But they do not dispute Laurentian's submission that this issue was not argued

below. It is difficult to fault the CCAA judge for not weighing a competing interest that was not asserted before him.

[35] The moving parties also say that the CCAA judge failed to advert to the impact his ruling would have on freedom of expression. We are satisfied he did take that factor into account, as he mentions it in setting out the test and later says that the deleterious effects include “the public interest in accessing the Exhibits.”

[36] The second and third questions raised by the moving parties ask the court to revisit an issue raised before the CCAA judge. He described the essence of the submissions made to him by those opposing the sealing order as there being no evidence that the sealing order was necessary to protect a valid commercial interest.

[37] The CCAA judge was satisfied that there was a sufficient evidentiary basis. He based his conclusion that disclosing the Exhibits posed a serious risk to the restructuring on his review of the Exhibits and Dr. Haché’s evidence. The moving parties are correct that Dr. Haché did not opine in his affidavit that disclosure of the Exhibits posed a serious risk to the viability of the restructuring. But Dr. Haché’s evidence describes something of the dynamics at play and is clear as to Laurentian’s dire position and the timeframe within which the restructuring must be completed, if it is to be successful. It provided the foundation on which the

Monitor, an officer of the court, supported Laurentian's position that disclosure posed a serious risk, and the CCAA judge, who has extensive experience in CCAA restructurings, concluded that disclosure posed a serious risk. The CCAA judge exercised his judgment, based on an evidentiary record.

[38] The fact the proposed appeal is not *prima facie* meritorious weighs significantly against granting leave.

Appeal Would Hinder Progress of the Action

[39] As we have said, this restructuring is on an exceptionally short timeline. We are told that the mediation is ongoing, with sessions occurring daily. There is urgency to being able to reach a successful restructuring by the end of April, in light of Laurentian's financial position and the need for certainty regarding the next academic year. There is too great a risk that an appeal would be a distraction from restructuring efforts and thus would unduly hinder the progress of the action, which also weighs significantly against granting leave.

No Significance to the Action

[40] Given the involvement of a court-appointed mediator and that it is open to the CCAA judge to revisit the sealing provision and possibly revoke it or limit its impact by allowing the parties to the CCAA proceeding to access the sealed documents, the significance of the proposed appeal to the action is insufficient to justify leave.

Significance to the Practice

[41] The facts of this case highlight some novel and interesting questions about the application of the *Sierra Club* test in the CCAA context.These include questions about granting sealing orders over information filed in support of the application for protection under the CCAA, the granting of sealing orders where interests under s. 2(d) of the *Charter* are arguably at play, and about the application of sealing orders to parties and stakeholders involved in the restructuring efforts. However, given our view of the merits of the proposed appeal and the other factors, this is not the appropriate case in which to explore these issues.

Disposition

[42] Leave to appeal is refused. In the circumstances, there shall be no order as to costs.

Pepall JA

B Zarnett JA

TAB 5

Citation: Doman Industries et al 2004 BCSC 733

Date: 20040525
Docket: L023489
Registry: Vancouver

IN THE SUPREME COURT OF BRITISH COLUMBIA

Oral Reasons for Judgment
The Honourable Mr. Justice Tysoe
Pronounced in Chambers
May 25, 2004

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

AND

IN THE MATTER OF THE *COMPANY ACT*
R.S.B.C. 1996, c. 62

AND

IN THE MATTER OF THE *CANADA BUSINESS CORPORATIONS ACT*
R.S.C. 1985, c. C-44

AND

IN THE MATTER OF THE *PARTNERSHIP ACT*
R.S.B.C. 1996, c. 348

AND

IN THE MATTER OF DOMAN INDUSTRIES LIMITED,
ALPINE PROJECTS LIMITED,
DIAMOND LUMBER SALES LIMITED, DOMAN FOREST PRODUCTS LIMITED,
DOMAN'S FREIGHTWAYS LTD., DOMAN HOLDINGS LIMITED,
DOMAN INVESTMENTS LIMITED, DOMAN LOG SUPPLY LTD.,
DOMAN–WESTERN LUMBER LTD., EACOM TIMBER SALES LTD.,
WESTERN FOREST PRODUCTS LIMITED,
WESTERN PULP INC.,
WESTERN PULP LIMITED PARTNERSHIP,
and QUATSINO NAVIGATION COMPANY LIMITED

PETITIONERS

Counsel for the Petitioner, Western Forest Products Ltd.:	E.J. Harris, Q.C. and P.D. McLean
Counsel for Hayes Forest Services Ltd.:	I.G. Nathanson, Q.C. and S.R. Schachter, Q.C.
Counsel for Tricap Restructuring Fund:	M.I. Buttery
Counsel for Strathcona Contracting Ltd.:	S.R. Ross
Counsel for Committee of Unsecured Noteholders:	K. Zych
Counsel for Petro-Canada Inc.:	C.E. Hirst

[1] **THE COURT:** One of the Petitioners, Western Forest Products Ltd., ("Western") applies, in these proceedings under the ***Companies Creditors Arrangement Act*** (the "***CCAA***") involving the Doman group of companies, for authorization or approval of the termination of contracts it has with Hayes Forest Services Ltd. ("Hayes") and Strathcona Contracting Ltd. ("Strathcona").

[2] The Doman group of companies ("Doman") carry on business in the B.C. forestry industry. Doman encountered financial difficulties and has been in the process of attempting to restructure under the ***CCAA*** for approximately one and a half years. The liabilities of ***Doman*** consist of secured term debt in the principal amount of U.S. $160 million, unsecured term notes in the principal amount of U.S. $513 million, unsecured

trade debt in excess of $20 million, a secured operating line of credit and other miscellaneous obligations.

[3] The restructuring process is nearing completion. A plan of compromise and arrangement (the “Restructuring Plan”) has been filed and the meeting of creditors to consider it has been scheduled to be held in approximately two weeks. The deadline for creditors to file proofs of claim is today.

[4] In very simple terms, the Restructuring Plan contemplates that the lumber and pulp assets of Doman will be transferred into new corporations and that the unsecured noteholders, trade creditors and other unsecured creditors will have their debt converted into shares in one of the new corporations, which will own the lumber assets and the shares of the other corporation holding the pulp assets. The secured term debt is to be refinanced and the secured operating line of credit will be unaffected. The existing shareholders of Doman are to receive warrants entitling them to purchase a limited number of shares in the new parent corporation.

[5] The implementation of the Restructuring Plan is subject to the fulfilment of numerous conditions precedent. One of the conditions is the termination of the contracts with Hayes and Strathcona which are the subject matter of this application.

[6] Western holds certain forest tenure, including licenses relating to an area known as the Nootka Region on Vancouver Island and at least one island off the coast of Vancouver Island called Nootka Island. In 1991, the B.C. government decided that logging contractors should have a form of security similar to the tenure enjoyed by license holders and created the concept of replaceable contracts under the ***Forest Act***.

[7] The attributes of replaceable contracts were discussed at length by the B.C. Court of Appeal in ***Clear Creek Contracting Ltd. v. Skeena Cellulose Inc.*** 2003 BCCA 344 and I will not repeat all of them here. In short, a replaceable contract is a form of evergreen contract which contains statutorily mandated provisions, the most important of which is that the license holder must offer a new or replacement contract to the contractor upon each expiry of the term of the contract as long as the contractor is not in default under the contract. If the parties are not able to agree on the new rates under the replacement contract, an arbitrator will determine the rates, which are mandated to be competitive within the industry and to permit the contractor to earn a reasonable profit on top of its costs. The contractors with such contracts are known in the industry as Bill 13 contractors. A

license holder must have at least 50% of its annual allowable cut harvested by Bill 13 contractors.

[8] Western has 7 full-phase Bill 13 logging contracts with 6 contractors for the Nootka Region. Hayes is one of those contractors and it has the full-phase contract for the Plumper Harbour area of the Nootka Region. A full-phase contract includes all aspects of logging ranging from road construction, falling, hauling, sorting and delivery to transportation points. Hayes sold the road construction aspect of its contract, and the replaceable contract for road construction was assigned to Strathcona.

[9] When Doman first commenced these ***CCAA*** proceedings, it was anticipated that the restructuring process would be completed in a relatively short period of time. It was contemplated that all unsecured debt other than the unsecured bondholders would be paid in full and that the unsecured bondholders would take most, but not all, of the equity in Doman in exchange for some of the indebtedness owed to them and would take security for the remainder of their indebtedness. The confirmation or come-back Order of December 6, 2002 authorized a downsizing process for Doman, but it was not instituted in view of the anticipated restructuring.

[10] The restructuring initially contemplated by Doman did not take place, in part because I made a ruling that the covenants in the trust deed for the secured term debt could not be overridden into the future. By the beginning of April 2004, the unsecured bondholders were pressing for their own restructuring plan and had made it clear that there should be some downsizing in Doman's operations, particularly the closure of Doman's pulp mill in Port Alice. On April 6, 2004, I declined Doman's application for an extension of the stay for the sole purpose of pursuing refinancing of its debt and the sale of the Port Alice pulp mill, but I also declined an application of the unsecured bondholders to call a meeting of creditors to consider its plan of arrangement. I extended the stay for the purpose of allowing Doman to file its own restructuring plan while still pursuing refinancing and sale alternatives, but I imposed a fairly concrete deadline by directing that the creditors meeting be held on June 7. In my April 6 Order, I authorized Doman to reinstitute its downsizing process with special emphasis on the closure of the Port Alice pulp mill if a purchaser was not located. I also placed a restriction on any downsizing by providing that any termination of a replaceable contract under the ***Forest Act*** was not to be effective unless authorized by the court.

[11] By letters dated April 27, 2004, Western terminated its contracts with Hayes and Strathcona effective upon court approval of the terminations. An affidavit of Mr. Zimmerman, a Western employee, provided the following rationale for the decision to terminate these replaceable contracts:

> As part of the reorganization and “downsizing” processes of [Western], we have looked at methods to rationalize harvesting operations in the Nootka Region so as to reduce costs and improve profitability of [Western]. [Western] has worked in conjunction with representatives of the Bondholder committee who have asked for recommendations so as to increase profitability. [Western] has determined that within the Nootka Region, operational efficiencies can be achieved and significant cost savings can be achieved if the number of contractors is reduced and if that contractor’s allocated volume is re-allocated to the remaining contractors. [Western] has recommended this reduction to the Bondholders Committee and the representatives of the Committee have asked that [Western] institute a rationalization and termination of contract, which is subject to Court approval as provided in this Court’s Order of April 6, 2004.

The affidavit goes on to state that the rationalization can best be carried out by the termination of the Plumper Harbour contracts, principally because the contractor costs associated with this location are the highest in the Nootka Region. The volume under the contracts would then be re-allocated to other Bill 13 contractors in the Nootka Region. The average contract rate for logging a cubic metre of timber under the Hayes contract for the period from 1998 to 2001, as determined by arbitration, was approximately $4 higher than the average rate under the other contracts for the Nootka Region.

[12] Mr. Zimmerman's affidavit indicated that Western did not intend to harvest at Plumper Harbour for the next three years and set out the savings that Western would be able to achieve by terminating the Hayes and Strathcona contracts. These savings were estimated at $5 million over the next three years and $800,000 for each year thereafter. These included annual savings of approximately $165,000 in road building costs, but the main reason Western wants to terminate its contract with Strathcona is that the full-phase contractor replacing Hayes may have its own road building capabilities. Mr. Zimmerman also exhibited to his affidavit a proposal which Hayes had made to Western in 1999 whereby Hayes offered to exchange its rights under its Bill 13 contract for the exclusive right to do helicopter logging in the Nootka Region with an annual minimum guarantee. In the proposal, Hayes stated that the average cut for many of the Bill 13 contractors had been reduced below an efficient economic operating level and that higher costs were being passed on to Western. The proposal was not accepted by Western because it did not want to give exclusive rights for helicopter logging with a guaranteed entitlement.

[13] Representatives of Hayes and Strathcona swore affidavits disputing that the savings would be of the magnitude estimated by Mr. Zimmerman. They also set out the prejudice which their companies would suffer if the contracts were terminated, including the loss of employment and the inability to utilize fixed assets. Mr. Hayes deposed that there is no reasonable or rational economic reason for Western to forego harvesting in Plumper Harbour this year because most of the engineering and road construction costs have already been incurred. Mr. Hayes estimated that if Western harvested the timber on its logging plan for this year in Plumper Harbour, it would receive revenue, net of additional harvesting costs, of approximately $2 million.

[14] The affidavit of Mr. Hayes also stated that Hayes recognized that the operations of the Bill 13 contractors in the Nootka Region are inefficient, unwieldy and costly. Despite this acknowledgment, Mr. Hayes expressed a view that the termination of its contract will not have a material impact on cost reduction in the Nootka Region when one takes into account that the Province will be taking back approximately 20% of Western’s annual allowable cut in the Nootka Region pursuant to the recently enacted ***Forestry Revitalization Act*** and will thereby cause a reduction in the

volumes harvested by all of the Bill 13 contractors. No affidavit was sworn by a Western representative to dispute this statement.

[15] Mr. Zimmerman, Mr. Hayes and the deponent on behalf of Strathcona were cross-examined on their affidavits. In his cross-examination, Mr. Zimmerman stated that Western did intend to liquidate the developed timber at Plumper Harbour of approximately 130,000 cubic metres over the next two years before putting the area in abeyance for a three year period. Western has not introduced any evidence with respect to the anticipated costs if this developed timber is harvested or is harvested by other Bill 13 contractors rather than Hayes.

[16] In addition to the ***Skeena Cellulose*** decision which dealt with the termination of replaceable contracts in ***CCAA*** proceedings, counsel referred me to several other cases involving the termination of contracts, leases or licenses in ***CCAA*** proceedings.

[17] In ***Re Dylex Ltd.,*** [1995] O.J. No. 595 (Q.L.) (Ont. Ct. of Jus.), Farley J. authorized the insolvent company to repudiate the leases of three of its stores as part of a program to close 200 of its stores across Canada. The three stores had been a financial drain on Dylex. Although the closures were going to have a detrimental effect on the shopping centres in

which the stores were located, Farley J. held that in weighing the balancing of interests in a ***CCAA*** context, the court's discretion should be exercised in favour of Dylex over the landlord, which was in sound financial condition. Farley J. declined to import into the ***CCAA*** the requirement applicable to proposals under the ***Bankruptcy and Insolvency Act*** that the insolvent company has to show that it would not be able to make a viable proposal unless it terminated the leases in question.

[18] In ***Re Blue Range Resource Corp.*** 1999 ABQB 1038, the insolvent company had been authorized by the court under the initial stay order to terminate such of its contracts as it deemed appropriate to permit it to proceed with an orderly restructuring of its business. Blue Range terminated some of its natural gas supply contracts and three of the parties to such contracts sought to challenge the termination of their contracts. One of the issues they raised was that the stay order should be varied to provide that Blue Range would only be permitted to terminate the contracts if it was incapable of performing them or if the termination was essential to the success of their restructuring. Lo Vecchio J. dismissed the application to vary the stay order in this fashion. He made

the following comments at paras. 36 through 38, which have been quoted in subsequent cases:

> The purpose of the CCAA proceedings generally and the stay in particular is to permit a company time to reorganize its affairs. This reorganization may take many forms and they need not be listed in this decision. A common denominator in all of them is frequently the variation of existing contractual relationships. Blue Range might, as any person might, breach a contract to which they are a party. They must however bear the consequences. This is essentially what has happened here.
>
> A unilateral termination, as in any case of breach, may or may not give rise to a legitimate claim in damages. Although the Order contemplates and to a certain extent permits unilateral termination, nothing in Section 16.e or in any other part of the Order would suggest that Blue Range is to be relieved of this consequence; indeed Blue Range's liability for damages seems to have been assumed by Duke and Engage in their set-off argument. The application amounts to a request for an order of specific performance or an injunction which ought not to be available indirectly. In my view, an order authorizing the termination of contracts is appropriate in a restructuring, particularly given that it does not affect the creditors' rights to claim for damages.
>
> The Applicants are needless to say not happy about having to look to a frail and struggling company for a potentially significant damages claim. They will be relegated to the ranks of unsecured judgment creditors and may not, indeed likely will not, have their judgments satisfied in full. While I sympathize with the Applicants' positions, they ought not to, in the name of equity, the guide in CCAA proceedings, be able to elevate their claim for damages above the claims of all the other unsecured creditors through this route.

[19] Lo Vecchio J. held that the court has the necessary jurisdiction to permit termination of contracts and that the termination of the contracts in question was necessary to the company's survival program.

[20] In ***Re T. Eaton Co.***, [1999] O.J. No. 4216 (Q.L.) (Ont. Sup. Ct. of Jus.), Farley J. refused to order specific performance of an exclusive license to provide credit card services that had been repudiated by the insolvent company as part of a sale of its assets which was the foundation of its restructuring plan. He held that the licensee could be adequately compensated in damages and should not have a higher claim than any other unsecured creditor. In the course of his reasons, he quoted the above portions of the ***Blue Range*** decision, and said the following at para. 7:

> It is clear that under CCAA proceedings debtor companies are permitted to unilaterally terminate in the sense of repudiate leases, and contracts without regard to the terms of those leases and contracts including any restrictions conferred therein that might ordinarily (i.e. outside CCAA proceedings) prevent the debtor company from so repudiating the agreement. To generally restrict debtor companies would constitute an insurmountable obstacle for most debtor companies attempting to effect compromises and reorganizations under the CCAA. Such a restriction would be contrary to the purposive approach to CCAA proceedings followed by the courts to this date.

Farley J. also spoke about being cognizant of the function of a balancing of prejudices within the general approach to the ***CCAA***.

[21] The issue of the court's jurisdiction to authorize the termination of replaceable contracts under the ***B.C. Forest Act*** was first addressed in the predecessor to the ***CCAA*** proceedings of Skeena Cellulose, ***Re Repap British Columbia Inc.,*** June 11, 1997, Docket No. A970588 (B.C.S.C.). Thackray J. held that the court had the jurisdiction under the ***CCAA*** to authorize the insolvent company to terminate replaceable contracts. None of the replaceable contracts in question were actually terminated until the subsequent Skeena Cellulose proceedings.

[22] In the Skeena Cellulose proceedings, the come-back order authorized the company to terminate replaceable contracts in order to facilitate the downsizing and consolidation of its business and operations. As part of Skeena Cellulose's plan of compromise and arrangement, a third party agreed to purchase the shares in the company for $8 million, which was to be used for distribution to the creditors having claims in excess of $400 million. It was a condition precedent to the purchase that two of Skeena Cellulose's five replaceable contracts be terminated, and letters of termination were sent.

The two contractors applied to the court for a declaration that the terminations were invalid.

[23] Brenner C.J.S.C. dismissed the application. In his decision (cited at 2002 BCSC 1280), he said the following at para. 25:

> SCI has no authority to decline to replace the applicants' replaceable contracts under the terms of those contracts, or in accordance with the provisions of the Regulation that deal with when and how a replaceable contract can be terminated. The only authority for SCI to terminate, or indeed, jurisdiction for this court to approve such terminations, must be found in the terms of the Come-back Order, and in the provisions of the CCAA. To be effective, the terminations must:
>
> (a) comply with the procedures and conditions stipulated in the Come-back Order; and,
>
> (b) conform to the broader principles of economic necessity and fairness which underlie the court's discretionary jurisdiction under the CCAA.

Brenner C.J.S.C. expressed the view that the statutory privileges given to the Bill 13 contractors are not sufficient to justify the creation or recognition of a preference in favour of the contractors over other creditors.

[24] The appeal from Brenner C.J.S.C.'s decision was dismissed. In its decision, the B.C. Court of Appeal held that the court had an equitable jurisdiction to supplement the ***CCAA*** by approving a plan of arrangement which contemplates the

termination of contracts by the debtor corporation. Newbury J.A. held that in approving such a plan involving the termination of replaceable contracts, the court was not overriding provincial legislation because nothing in the legislation purported to invalidate a termination of a replaceable contract but that, in any event, the doctrine of paramountcy would result in preference being given to the ***CCAA*** over the ***B.C. Forest Act*** in the case of a conflict.

[25] The Court of Appeal found no error in the exercise of discretion by Brenner C.J.S.C. Newbury J.A. said the following about the concept of fairness at para. 60:

> I have no difficulty in accepting the appellants' argument that fairness as between them and the other three evergreen contractors and as between the appellants and Skeena was a legitimate consideration in the analysis of this case. (Indeed, I believe the Chief Justice considered this aspect of fairness, even though he did not mention it specifically in this part of his Reasons.) The appellants are obviously part of the "broad constituency" served by the CCAA. But the key to the fairness analysis, in my view, lies in the very breadth of that constituency and wide range of interests that may be properly asserted by individuals, corporations, government entities and communities. Here, it seems to me, is where the flaw in the appellants' case lies: essentially, they wish to limit the scope of the inquiry to fairness as between five evergreen contractors or as between themselves and Skeena, whereas the case-law decided under the CCAA, and its general purposes discussed above, require that the views and interests of the "broad constituency" be considered. In the case at bar, the Court was concerned with the

> deferral and settlement of more than $400 million in debt, failing which hundreds of Skeena's employees and hundreds of employees of logging and other contractors stood to lose their livelihoods. The only plan suggested at the end of the extended negotiation period to save Skeena from bankruptcy was NWBC's acquisition of its common shares for no consideration and the acceptance by its creditors of very little on the dollar for their claims.

The Court of Appeal concluded that there was a business case for the terminations. Newbury J.A. stated that the situation in ***Dylex*** was no different in principle because, like the leases in ***Dylex***, the replaceable contracts were too costly for Skeena Cellulose to continue operating under them.

[26] Although the Court of Appeal's decision in ***Skeena Cellulose*** settles that the court has the necessary jurisdiction to deal with the termination of contracts, none of the above decisions includes any detailed discussion with respect to the basis upon which the court becomes involved in decisions to terminate contracts. Newbury J.A. discussed the jurisdiction in terms of the court approving a plan of arrangement which involves the termination of contracts, but the court will often authorize the termination of contracts prior to the formulation of a plan of arrangement.

[27] If a debtor company repudiated a contract prior to commencing ***CCAA*** proceedings, the court would not have any direct involvement in the termination of the contract unless,

possibly, the other party to the contract sought specific performance of the contract (which, as Brenner C.J.S.C. pointed out in ***Skeena Cellulose,*** is particularly inappropriate in an insolvency). The other party to the contract would have a claim for damages in respect of the repudiation and would be treated like any other unsecured creditor for the purposes of the plan of arrangement.

[28] Once an insolvent company seeks the assistance of the court by commencing ***CCAA*** proceedings, the company comes under the supervision of the court. The supervision also involves a consideration of the interests of the broad constituency served by the ***CCAA*** mentioned in ***Skeena Cellulose*** by Newbury J.A. These interests, when coupled with the exercise by the court of its equitable jurisdiction, bring into play the requirements for fairness and reasonableness in weighing the interests of affected parties.

[29] Generally speaking, the indebtedness compromised in ***CCAA*** proceedings is the debt which is in existence at the time of the ***CCAA*** filing, and the debtor company is expected to honour all of its obligations which become owing after the ***CCAA*** filing. It is common for the initial stay order or the come-back order to provide that the debtor company is to continue

carrying on its business and to honour its ongoing obligations unless the court authorizes exceptions.

[30] In many reorganizations under the ***CCAA,*** it is necessary for the insolvent company to restructure its business affairs as well as its financial affairs. Even if the financial affairs are restructured, the company may not be able to survive because portions of the business will continue to incur ongoing losses. In such cases, it is appropriate for the court to authorize the company to restructure its business operations, either during the currency of the ***CCAA*** proceedings or as part of a plan of arrangement. The process is commonly referred to as a downsizing if it involves certain aspects of the business coming to an end. The liabilities which are incurred as a result of the restructuring of the business operations, for such things as termination of leases and other contracts, are included in the obligations compromised by the plan of arrangement even though the debtor company will have been honouring its ongoing commitments under the leases and other contracts after the commencement of the ***CCAA*** proceedings. The inclusion of these liabilities in the plan of arrangement is an exception to the general practice of debtor companies paying the full extent of post-filing liabilities and compromising only the pre-filing liabilities.

[31] It is within this context that the court is called upon to authorize the termination of contracts which the debtor company could have repudiated without any authorization prior to the commencement of ***CCAA*** proceedings. The liabilities to be compromised have, in general terms, been crystallized by the filing of the ***CCAA*** petition, and the affairs of the debtor company are under the supervision of the court, which is required to exercise its equitable jurisdiction fairly and reasonably.

[32] I do not approach the matter in the same fashion as Lo Vecchio J. did in ***Blue Range***. I do not see the resistance of a party to the termination of a contract with the debtor company to be an attempt to elevate their claim for damages above the claims of all the other unsecured creditors. Apart from any monies which may have been outstanding under the contract at the time of the ***CCAA*** filing, the party to the contract was not an unsecured creditor who was going to be subjected to a compromise under a plan of arrangement. The party only becomes a creditor in respect of its damage claim if the contract is terminated. Although Lo Vecchio J. could be interpreted as suggesting in the quoted paragraphs 36 to 38 that a debtor company may terminate contractual relations as long as the resulting damage claim is included in its plan of

arrangement, I do note that he subsequently commented that the termination of the contracts in that case was necessary to the company's survival program.

[33] I prefer the approach of Farley J. in ***Dylex,*** which involves the court weighing the competing interests and prejudices in deciding what is fair and reasonable. I would anticipate that in the majority of cases a debtor company will be able to persuade the court to exercise its discretion in favour of the termination of contracts and other steps required to downsize or rationalize its business affairs. A debtor company must be insolvent to qualify under the ***CCAA*** and the insolvency may have been caused by over-expansion or continual losses by a part of the business. If the company is to have a reasonable prospect of surviving into the indefinite future, it will be appropriate to downsize its operations or bring an end to the losing aspects of the business. The interests of the broad constituency of stakeholders in taking reasonable steps to ensure the ongoing viability of the business will often outweigh the prejudice caused to parties having their contracts or other arrangements with the debtor company terminated and their consequential damage claim being included in the plan of arrangement. There is no single test for the debtor company to satisfy apart from demonstrating

that the termination is fair and reasonable in all of the circumstances. As held in ***Dylex***, it is not necessary for the debtor company to demonstrate that the termination of the contract is essential to the making of a viable plan of arrangement.

[34] An example of this type of situation has already occurred in these proceedings. Doman's pulp mill at Port Alice has been losing money for a significant period of time and causing a financial drain on Doman's resources. At the suggestion of the bondholders, it was decided that the mill should be closed and should not be part of the restructured company. Although the closure of the mill would have had a devastating effect on the employees of the pulp mill and the Village of Port Alice as a whole, I authorized the closure because it would not have been reasonable to require the restructured company to operate a division of its business which was anticipated to continue to lose money. Fortunately, Doman was able to find another party who was willing to take over the pulp mill prior to its closure.

[35] On the other hand, there will be circumstances where it will not be appropriate to authorize the debtor company to terminate contracts. For example, suppose that a debtor company became insolvent because its business had been

operating at a loss but market conditions had changed and, with a financial restructuring of its existing debt, it was expected to be profitable in the future. Suppose further that the debtor company was party to a contract which did not cause the company to operate the relevant aspect of its business at a loss but the contract was not as favourable as the market would permit the company to obtain if it could divest itself of the existing contract. If the company could terminate the contract and enter into a new one with different rates, it could become substantially more profitable into the future. In these circumstances, it may well be inappropriate for the court to authorize the termination of the contract. The risk of the failure of the debtor company after its restructuring would be relatively low and, depending on the terms of the plan of arrangement, the future benefit of the contract termination may accrue to the shareholders of the company or to the creditors of the company who took risks in exchange for high rates of return.

[36] On the present application, all that the evidence establishes is that Doman will likely be able to reduce its costs to some extent at some point in the future if it can terminate the two contracts in question. Mr. Zimmerman’s affidavit states that the reason Western made the

recommendation to terminate the two contracts was to improve or increase its profitability. There is no evidence on this application with respect to the following points:

(a) whether the logging at Plumper Harbour under the existing contracts has produced a loss in the past or is expected to produce a loss in the future;

(b) whether other logging operations of Doman produce a greater loss;

(c) whether other aspects of Doman's business produce a loss and, if so, what consideration has been given to rationalizing that loss in comparison to the termination of the contracts in question;

(d) whether it is expected that the restructured company will operate at a profit;

(e) what parts of the constituency of stakeholders will benefit from the termination of the contracts in question;

(f) whether the developed timber at Plumper Harbour can be harvested in the next two years by other contractors at a cost less than the cost under the contracts in question; and

(g) what is the fallacy, if any, in the assertion of Mr. Hayes that the termination of the contracts will have no material impact on cost reduction after taking into account the 20% government take-back.

[37] Some reliance was placed by counsel on the fact that the termination of these contracts is a condition precedent of the Restructuring Plan. In my view, this condition precedent is materially different than the condition precedent in ***Skeena Cellulose***. In that case, it was an independent purchaser of the shares in ***Skeena*** that negotiated the condition on the basis that it was not prepared to purchase the shares unless two of the five replaceable contracts were terminated. The condition resulted from an arm’s length negotiation which required the purchaser to put up funds to purchase the shares. In the present case, the bondholder committee produced the initial draft of the Restructuring Plan, which was finalized after a limited negotiation that served to advance the interests of the existing directors and shareholders of Doman. The condition precedent in question was not contained in the initial draft of the Restructuring Plan put forward by the bondholders and there is no evidence as to why the condition was inserted in the Restructuring Plan. I am unable to conclude that the condition precedent was the result of a

truly adversarial negotiation and that, unlike the situation in ***Skeena Cellulose,*** the restructuring is unlikely to proceed if the condition is not satisfied.

[38] In my opinion, therefore, there is insufficient evidence for me to conclude that the proposed contract terminations are fair and reasonable in all of the circumstances. All that the evidence available to me supports is a conclusion that the restructured company will have an opportunity of being more profitable if the contracts are terminated. It has not been demonstrated that the loss of this opportunity will outweigh the prejudice which will be suffered by Hayes and Strathcona if the contracts are terminated. In weighing the competing interests on the evidence before me, it is my conclusion that I should exercise my discretion against approving the contract terminations. I dismiss the application with costs.

"D.F. Tysoe, J."
The Honourable Mr. Justice D.F. Tysoe

TAB 6

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Insolvency Institute of Canada (Articles)

— Recent Trends in DIP Financing

——*Waël Rostom and Caitlin Fell* *

1. INTRODUCTION

When an insolvent company contemplates filing for protection under one of Canada's principle restructuring statutes, it may require interim financing or, as more typically referred to, debtor in possession (DIP) financing. DIP financing should provide the applicant company with sufficient liquidity to fund its operations and to cover the costs of the court-supervised proceedings while the applicant company attempts to successfully restructure its business. The availability of reliable DIP financing can also help to increase stakeholder confidence in the company's restructuring efforts, which may in turn lead to greater cooperation by stakeholders. The availability of, and allowance for, DIP financing under the *Companies' Creditors Arrangement Act* [2] (CCAA) and the proposal provisions of the *Bankruptcy and Insolvency Act* [3] (BIA) is intended to reflect and complement the statutory objectives of the CCAA and proposal provisions of the BIA, which are to allow a debtor time and breathing space to facilitate a going concern solution that maximizes value for the benefit of all stakeholders. Thus, where a company requires DIP financing, the selection of the DIP lender and the terms and conditions of the financing will be crucial decisions.

While DIP financing is far from a new phenomenon in Canada, recent CCAA cases involving companies financed by DIP loans have shed light on several emerging issues and trends in DIP lending. This paper will explore these recent issues and trends, including DIP loan terms and pricing, issues pertaining to DIP lender control in a proceeding and whether a competitive DIP loan selection process should be required. This paper will also explore the current uncertainty in the judicial treatment of roll-ups and creeping roll-ups. These cases provide restructuring professionals and lenders with important guidance on how to properly structure DIP financing in practice and ultimately maximize the chances of successfully obtaining court approval.

In addition, the authors argue that adequate notice of more than just a few days for a motion to approve DIP financing is required to ensure procedural fairness. Adequate notice should permit stakeholders time to review the detailed terms and conditions of the DIP financing proposal, its impact on their position and the restructuring proceedings more generally, and time to prepare any responding materials. This simple procedural step should impose more discipline on the moving party to rely on substantive justification for the specific terms and conditions of the proposed DIP financing sought and mitigate the over-reliance that is frequently placed on factors such as "urgency" and expediency. The authors have observed that Canadian courts are increasingly viewing assertions of urgency with greater skepticism, recognizing that sometimes emergencies are self-made. Courts should impose and guard adequate notice requirements to encourage meaningful consultation by the debtor and proposed DIP lender with major stakeholders.

2. BACKGROUND OF DIP FINANCING

While DIP financing was only codified in the CCAA and BIA in 2009, previously courts nonetheless approved DIP financings on the basis of their inherent jurisdiction. [4] Effective in 2009, Parliament codified the use of interim financing and the test to be applied by the court in approving DIP financing. Section 11.2 of the CCAA grants the court the ability to approve interim financing, and a corresponding charge in favour of a DIP lender, in an amount that is required by the debtor, having regard to its cash-flow statement. [5] The application by the debtor for DIP financing must be with notice to any secured creditors likely to be affected. Section 11.2(4) sets out a non-exhaustive list of factors to be considered by the court in determining whether to grant an order approving DIP financing. In deciding whether to grant such order, the court is to consider, among other things:

- the period during which the company is expected to be subject to proceedings under the CCAA;
- the management of the company's business and financial affairs during the proceedings;
- whether the company's management has the confidence of its major creditors;
- whether the loan would enhance the prospects of a viable compromise or arrangement being made in respect of the company;
- the nature and value of the company's property;
- whether any creditor would be materially prejudiced as a result of the security or charge; and
- the monitor's report referred to in paragraph 23(1)(b) of the CCAA, if any. [6]

Since the codification of DIP financing, trends have emerged which have spurred debate on how to properly balance the necessity for protections of a DIP lender to encourage lending in an insolvency situation with the interests of the debtor and other stakeholders. These competing interests are not new in Canada or the United States. However, the balancing of these interests becomes particularly important at a time when commodity prices are dangerously low and when some Canadian debtors are severely impacted by the decline in the Canadian dollar. Current market conditions put in jeopardy the value of recovery for existing creditors and, in some cases, even the DIP lenders themselves. Increased tensions between the rights of DIP lenders and the objectives of the CCAA are resulting in justifiably greater oversight and direction by the court in setting the standard of fairness within the circumstances of each CCAA case.

3. OBSERVATIONS ON DIP PRICING

When approving a DIP loan, courts will consider the reasonableness of the financing terms and the fees charged by the DIP lender. As mentioned by the Court in *Canwest Publishing Inc./Publications Canwest Inc., Re*, [7] there should be evidence presented to the court as to the reasonableness of the fees charged by the DIP lender. Increasingly, courts are turning to, and relying on, the monitor of the debtor for recommendations as to the terms and fees charged under the DIP loan. Generally speaking, courts will expect to see evidence that demonstrates that pricing and terms are better than, or equal to, other DIP proposals received by the debtor or that the DIP facility, and its terms are not out of line with comparable DIP facilities approved in other cases. [8] However, as discussed further below, pricing alone should not be the determining factor in the selection of a DIP loan.

The authors examined a sample of DIP financing cases in Canada between 2010 and 2015. The average fixed interest rate in the sample for DIP financing was approximately 10.75%, with a range of between 2% and 21%. With respect to floating or variable interest rate DIP financing, base rates included prime rate or LIBOR loans with or without floor base rates. It was not uncommon to see floor base rates in the range of 3% to 4%. In the sample, the average interest rate premium over the applicable base rates was approximately 6.08%, with a range of interest premium between 2% and 11%.

The pricing elements of DIP financing can also include all, or a combination of, commitment fees, unused line fees, cash pay interest, extension fees, exit fees, cost and professional fee reimbursements and other fees. Looking at a sample of DIP financing cases, the range of total upfront administration, structuring, closing or commitment fees charged by a DIP lender, in the period from 2011 to 2015, was between 2% and 14%. With respect to exit fees, DIP lenders in the sample charged a range of 2% to 6.15% during the same period. These pricing examples are intended to be illustrative only. The reality is that the Canadian DIP lending market is not robust enough to produce true "market" DIP interest rates and fees.

The pricing of DIP financing will be influenced by a number of factors, including macroeconomic conditions, industry conditions, company credit risk analysis, priority ranking of security for the DIP financing, cost of capital and investment hurdle rates for the DIP lender, motivations of the proposed DIP lender in providing the DIP loan and whether or not the company ran a competitive DIP financing selection process. The costs of a DIP loan will necessarily result in reduced cash available to the debtor or for net distributions to creditors. In addition, the circumstances under which some fees are triggered can have an impact on the options available to a debtor during the case. For example, some DIP loans include an exit fee payable to the DIP lender when the loans advanced are fully repaid. Some exit fees are simply deferred compensation to the DIP lender for a successful restructuring resulting in repayment of the DIP. However, the authors have observed some "exit fees" that appear to be to be payable in full, even if only $1 is advanced and then repaid under the DIP loan and payable on any refinancing of the DIP. This latter feature can have the effect of entrenching the incumbent DIP lender by making it very expensive to replace the DIP lender if relations sour at some point in the case. While there may be sufficient justification for such fees in the particular circumstance of a case, it is important for the debtor and the monitor to fully explain the impact of such fee arrangements to the court and other stakeholders. Certainly, there is a question as to whether an exit fee should become effective if the consideration of the DIP loan approval remains subject to determination on the comeback hearing, in case the initial DIP advance is repaid from a subsequently approved replacement DIP loan.

Courts must weigh the financial economics of the loan against other terms or conditions of a DIP loan, which may impose onerous controls on the debtor. For instance, the Court in *Cystallex* [9] approved a proposed DIP loan of $36 million that was more expensive and provided for fundamental changes to Crystallex's governance and capital structure over a competing $10 million DIP at a simple interest rate of 1% proposed by Crystallex's noteholders. [10] The competing noteholder DIP essentially provided for low cost interim financing without requiring fundamental changes to Crystallex's governance and capital structures. Notwithstanding the availability of a DIP with cheaper financial terms, the Court approved the more expensive DIP loan on the basis that it provided much more certainty. [11] The approved DIP provided committed funding until the expected conclusion of the restructuring whereas the proposed noteholder DIP only provided funding to a date by which Crystallex would need to have developed an acceptable restructuring proposal. [12] The risk to Crystallex was that, if the noteholders did not agree to provide the additional funding when needed, then Crystallex could be restricted in concluding a restructuring. Crystallex believed that it would be difficult for the company to return to the market to solicit DIP proposals if it needed additional funding, as financing sources would be reluctant to spend additional time and resources to submit another financing proposal. Further, the Court noted that the cheaper noteholder DIP with a 1% interest rate would only assist in removing, or seriously eroding, the chance of Crystallex going to the market in time for a new loan that could be comparable to the below market noteholder DIP, thereby making the company unduly beholden to the noteholders. [13]

4. DIP LENDING AS MEANS OF ASSERTING GREATER CONTROL

In addition to assessing the financial terms of each proposal, factors such as timing, prejudice, risk and uncertainty play a central role in approving a DIP loan, especially when the court is presented with a competing DIP. [14] The assessment of these factors has become important in light of the increasing scrutiny that some courts are giving to "control" provisions in the DIP loan documentation. DIP financing is not just a way for the company to finance its restructuring proceedings — it is, and will inevitably always be, a tool to facilitate greater control in the proceedings, whether by the debtor or the DIP lender.

A debtor may be advised to attempt to obtain a DIP loan that provides the maximum amount of flexibility to carry out its contemplated restructuring and thereby reduce the amount of control or influence that existing creditors might otherwise exert. On the other hand, an existing secured creditor viewing matters from its unique position in the capital structure may wish to provide DIP financing to mitigate some of the debtor's extraordinary powers in a CCAA and place added restrictions on the debtor's conduct in the case to obtain maximum recovery on their pre-filing exposure. Therefore, it is not uncommon for an existing first secured lender, that believes that its position might be potentially impaired by a runaway restructuring process, to offer a DIP loan to ensure that the process does not create further risk or that its collateral position will not be eroded. In contrast, a junior creditor whose position may be on the cusp of being "in the money", may wish to advance super-priority financing on the strength of the senior lenders' collateral, and may hope that a long and extended process may create new options for it to recover value on its out of the money position. In addition, an existing stakeholder or new lender may wish to advance the DIP loan as a "loan to own" acquisition strategy.

There is nothing inherently problematic with the foregoing rationales for when a creditor might provide DIP financing or in relation to a debtor's selection of a proposed DIP loan. However, the problem lies where the DIP loan is used as a tool to gain an inappropriate or overreaching level of control in the proceedings to the prejudice of other stakeholders. For example a DIP lender may try to use its senior secured DIP position to gain certain unfair advantages for its pre-filing position. While it should be expected that any existing stakeholder that offers to provide a DIP loan will be seeking certain advantages as a result of the loan, the emphasis of concern should be on unfair or inappropriate advantages. The phenomenon of overreaching control is not new and the detrimental implication of excessive lender control in a proceeding was articulated by a United States Court:

> Under the guise of financing a reorganization, the Bank would disarm the debtor of all weapons useable against it for the bankruptcy estate's benefit, place the debtor in bondage working for the bank, seize control of the reins of reorganization, and steal a march on other creditors in numerous ways. The financing agreement would pervert the reorganizational process from one designed to accommodate all classes of creditors and equity interests to one specifically crafted for the benefit of the bank and the debtor's principals who guaranteed its debt. [15]

In *Great Basin Gold Ltd., Re*, the Court acknowledged that DIP lenders employ leverage to control the process in order to obtain advantages relative to other stakeholders. Thus, there is a need for the court, as the role of gatekeeper, to ensure that the terms of a DIP loan are reasonable, especially in circumstances where a court is being asked to approve DIP financing on the basis of urgency: [16]

> I recognize that in some restructuring proceedings, certain stakeholders may use existing leverage, to the extent that they have it, to take advantage of the chaos and uncertainty that are inherent in these situations. Strategies might be employed to secure for themselves advantages that they would not otherwise obtain. These advantages inevitably come at the expense of other stakeholders in the proceedings. These advantages are also almost always Court approved so that they cannot be later revisited. In those circumstances, the Court must be constantly vigilant against such strategies. [17]

Specific overreaching control provisions can include the following:

- aggressively short milestones to run a sale process and to complete a transaction (presumably where there was sufficient liquidity to run a longer process) and failure to achieve such milestones constituting an event of default;
- restrictions on the borrower's ability to sanction a plan that does not provide for the payment in full of the DIP lender's pre-petition obligations;
- provisions which require a sale transaction to pay out the pre-filing debt of the DIP lender; or
- provisions which limit the discretion of the court.

Recently, there has been an increased focus by the courts on whether certain control features in DIP loan documents are overreaching. The approval by the court of DIPs containing onerous control terms necessarily results in a greater risk of these terms becoming market practice, and consequently, being used as precedents in future cases to approve such DIP proposals. Notably, the inclusion of overreaching control provisions recently resulted in the Court refusing to approve certain provisions in a DIP financing proposal in the CCAA proceedings of *Essar Steel Algoma Inc.* [18]

On November 9, 2015 (the "filing date"), Essar Steel and certain of its related affiliates filed for protection under the CCAA, at which time the Court approved senior secured DIP financing by a syndicate of lenders comprising of the pre-filing revolving lenders and certain of the pre-filing term lenders. [19] The initial order affidavit submitted by the debtor requested approval of a DIP loan, which had the support of the monitor. The monitor was of the opinion that the DIP agreement was the product of a rigorous and thorough bidding process between the debtor, the DIP lender and another competing bidder for the DIP facility. [20] The DIP loan contained certain milestones for the marketing and sale of Essar Steel's assets. These milestones and certain other onerous control provisions were the subject of opposition from subordinated stakeholders, including the senior secured noteholders and the junior noteholders. The basis of the opposition included the following covenants contained in the DIP loan:

• the requirement that Essar Steel file a motion for bidding and sales procedures before January 4, 2016 (approximately eight weeks from the filing date);

• the requirement that Essar Steel obtain an order from the Court approving the bidding and sales procedures (SISP) before January 11, 2016 (approximately nine weeks from the filing date);

• the requirement that Essar Steel obtain an order from the Court before May 1, 2016 (approximately 25 weeks from the filing date), approving a sale or investment transaction and authorizing the distribution of the proceeds from the sale or investment transaction to the DIP lenders in full for the obligations under the DIP agreement and the pre-petition lenders in an amount sufficient to pay in full the obligations under the pre-petition senior facilities;

• the requirement that Essar Steel complete the above sale or investment transaction and distributions outlined above before August 31, 2016 (approximately 42 weeks from the filing date), as potentially extended; and

• a provision which limited the Court's discretion by providing that on an event of default, and after giving of notice of an event of default, the only issues that may be raised by any party in opposition thereto being whether, in fact, an event of default has occurred.

The subordinated lenders opposed the DIP financing on the basis that the milestones would force Essar Steel to rush into a sale process at an early stage. This had the potential to impair the ability of the debtor to examine and develop a broad range of restructuring alternatives and paths to maximize value. In his endorsement, Newbould J. took issue with several aspects of the DIP loan and ultimately required that changes be made to the terms of the DIP facility, notwithstanding that the monitor supported the DIP.[21] In its endorsement, the Court noted that the proposed DIP was far from ideal and articulated concern with respect to the amount of control sought by the DIP lenders:

> I do not see the DIP lenders as being merely altruistic. Like any DIP lender, it is in their interest to take what they can get. Their interest, of course, in a situation such as this in which they are all ABL or Term lenders, is to see the business successfully restructure, but to be sure they work it on their terms as much as possible.[22]

In the endorsement, the Court specifically took issue with the following DIP term provisions:

• a provision which would cause an event of default unless a plan provided for either the payment in full in cash of all obligations under the pre-petition senior facilities; and

• a provision which limited the recourse of any party if an event of default were to occur, to raising the question as to whether, in fact, the event of default has occurred or is continuing.[23]

Newbould J. directed the parties to amend these provisions as well as the milestones based on the concessions negotiated between the parties, which included a 10-day moratorium before an event of default could occur for failing to meet the milestones.[24] At the November 19, 2015 hearing, the DIP lenders agreed to further amendments to provide Essar Steel with additional time to run a sales and investment solicitation process. The milestones in the amended DIP were as follows:

1. Essar Steel and its advisors develop a business plan acceptable to the required DIP lenders, including a pricing outlook, before February 1, 2016 (approximately 12 weeks from the filing date).

2. Essar Steel develop and obtain an order for the SISP seeking potential sale of or investment in its business by no later than February 1, 2016 (approximately 12 weeks from the filing date). Any purchase or investment offer under the SISP must contain a sufficient cash (or other consideration satisfactory to the required DIP lenders) component to repay all amounts owing under the amended DIP agreement, including the revolving and term loan components.

3. Essar Steel must use its best efforts to launch the SISP by February 15, 2016 and no later than March 1, 2016 (approximately 16 weeks from the filing date), if necessary and after consultation with the required DIP lenders.

4. The deadline for final offers under the SISP will be May 15, 2016 (approximately 26 weeks from the filing date). An extension may be granted, but never beyond June 1, 2016 (approximately 29 weeks from the filing date), with the consent of the monitor after consultation with the required DIP lenders or as determined by the Court.

5. Any transaction under the SISP must have court approval no later than 30 days after the final offer deadline (by June 14, 2016). Any plan of compromise or arrangement resulting from the SISP must have court approval no later than 60 days after the final offer deadline (by July 14, 2016).

6. Any sale transaction must close or any implementation of any plan of compromise must be in place by August 31, 2016 (approximately 42 weeks from the filing date). [25]

The issue of milestones in a DIP loan is generally the subject matter of intense negotiation between the debtor and the DIP lender. For the debtor, the obvious risks of tight milestones may be that the milestones: (i) do not facilitate a robust sale process; (ii) do not allow the debtor sufficient time to explore a stand-alone reorganization or other restructuring alternatives; and (iii) take advantage of a decline in the applicable markets without giving parties in interest a reasonable time to assess the likelihood that such markets will rebound during the CCAA proceedings. [26] Further, in accepting aggressive timelines in a DIP financing proposal, a court should be cognizant of the establishment of tight timelines if the debtor has not provided evidence typically required in a sale process approval motion. On a sale process approval motion, a debtor must demonstrate that a fair, open and competitive sale solicitation process that meets the *Soundair* test [27] can be implemented within the proposed milestone dates.

The authors contend that sale milestones in a DIP agreement are necessary since an expensive and prolonged process could simply serve to further erode value without any guarantee of a higher or better outcome at the end of such process. It is important for courts and stakeholders to appreciate that there is no simple answer to the length of time a debtor should be given to have an opportunity to restructure. The approval of milestones in a DIP should be based on evidence by the debtor and the monitor that the requested DIP milestones are informed by an analysis taking into account market conditions, the nature of the assets, any deterioration of the business or collateral over time, the liquidity of the debtor and whether the sale process milestones permit the debtor to carry out a competitive and commercially reasonable process. A monitor and the court should therefore be mindful of sale milestones in a DIP to ensure that these milestones are based on a sensible, rational and evidentiary based assessment of the circumstances of each company.

5. DIP SELECTION PROCESS

While it appears intuitive that a company will look to select the least expensive DIP financing proposal, the considerations in choosing a DIP proposal are rarely that simple. The authors find that the issues around non-pricing terms, such as control, timelines, milestones and roll-up features, to be potentially more challenging considerations in a DIP loan selection process.

In selecting an appropriate DIP financing proposal, it is an unfortunate reality that many companies wait far too long to do serious planning and structuring of a potential formal court-supervised restructuring, including to adequately solicit multiple proposals for DIP financing. While in some cases delay in engaging in serious planning might be justified, given the time, money and resources required to undertake a DIP selection process, many seasoned practitioners would agree that there is generally a strong bias by management to postpone contingency planning for far too long. The authors contend that some of the very issues that cause the most significant opposition from stakeholders or a court on a motion for approval of DIP financing might be avoided, or at least mitigated, with a proper DIP selection process and adequate time for a company and a proposed monitor to properly consider the financial and control features of each solicited DIP proposal.

To obtain a DIP with terms that assists a debtor in seeking a going concern solution, a debtor, with the assistance of a financial advisor, should look to run a competitive DIP selection process. This can be done prior to the commencement of CCAA proceedings, or after such time, if the debtor has sufficient cash and a filing under the CCAA without DIP financing will not prejudice the operations of the debtor.

In *Crystallex*, [28] the debtor, under the terms of the initial order, was authorized to pursue all avenues of interim financing of its business to permit it to proceed with an orderly restructuring. The initial order further provided that the best DIP offer, as determined by *Crystallex*, pursuant to the auction procedures, shall be afforded the protection of the *Soundair* [29] principles so that it would be too late to make topping offers after the bid deadline. [30] The *Soundair* principles require a court to consider and determine: (i) whether there has been sufficient efforts to obtain the best price; (ii) the interests of all parties; (iii) the efficacy and integrity of the process by which offers were obtained; and (iv) whether there has been unfairness in the working out of the process. [31] As a result of a robust financing solicitation process, Crystallex sought and obtained approval for a DIP loan that would allow it to pursue recovery for its creditors from the significant cash proceeds that were expected to be obtained from pursuing an arbitration award.

In *Crystallex*, the *Soundair* principles were cited, in part because the DIP loan included an investment feature but also to avoid last minute topping bids. The one challenge in strictly applying the *Soundair* principles to a DIP selection process is that it may not be feasible or desirable to seek DIP proposals from the full universe of possible lenders. A much more modest and targeted list of possible lenders should be sufficient in most cases. With suitable modifications, it may be beneficial for a court to consider the *Soundair* principles in evidencing the fairness of a process in the selection by a debtor of a suitable DIP financing proposal

The benefits of management running a DIP selection process are fairly obvious:

- a DIP selection process will hopefully identify more than one DIP option and management can review the identities of the proposed DIP lenders and the terms of multiple proposals to determine which DIP provides the best overall financing arrangements for the case;

- choosing between alternative DIP proposals provide the company with more leverage to negotiate and obtain better terms;

- a competitive process should impose discipline on pricing, reduce the cost of DIP financing and reduce the level of onerous control provisions; and

- the cost and disruption of potential last minute DIP proposals being presented for tactical reasons will be reduced.

The question of whether the DIP selection process should occur prior to or after the commencement of the case will depend on the facts and the debtor's financing needs. In any event, the decision as to how to proceed should be made early on to avoid missing out on the benefits of the process for the debtor and stakeholders and to avoid unnecessary "urgent" filings with one take-it-or-leave-it DIP proposal.

In implementing a DIP selection process, the authors contend that debtors and financial advisors must analyze not only the pricing and financial items of a DIP proposal but also the control provisions required by a DIP lender that may limit the debtor's options or ability to run a robust sale or restructuring process. The very fact that a reasonable competitive DIP process was run should demonstrate to the court and stakeholders that efforts were made to obtain the best and the most suitable proposal. Importantly, running a DIP selection process should assist with providing evidence to the court for the approval of the proposed successful DIP loan by providing highly relevant comparables in the specific case.

6. THUMBS UP OR DOWN FOR ROLL-UPS?

Roll-ups, and permutations thereof, continue to be hotly debated largely because there is a serious question under Canadian restructuring laws about the use and permissibility of "roll-up" DIPs.

Under a true roll-up, a DIP lender's pre-filing debt or a portion thereof is paid back using advances under the DIP financing, and the pre-filing debt is thereby "rolled" into the DIP facility. In addition to a true full or partial roll-up mentioned above, a DIP lender may also try to seek approval of a "creeping roll-up". Under a creeping roll-up, instead of DIP proceeds being used to pay down pre-filing obligations, a debtor's cash from operating during the CCAA proceedings is swept and used to pay down pre-filing obligations, and there is a corresponding draw on the DIP facility to fund further operations. More rigorous and carefully structured "creeping roll-ups" only sweep the receivables that existed on the filing date or that are generated from inventory that existed on the filing date.

The judicial treatment of roll-ups and creeping roll-ups is inconsistent as to their permissibility. With respect to full or partial roll-ups, the Court in the CCAA proceedings of *White Birch Paper Holding Co., Re* [32] approved DIP financing and a corresponding super-priority charge, notwithstanding that $50 million of the $140 million DIP facility would directly repay and discharge the pre-filing asset based revolving credit facility extended by the DIP lender. In approving the White Birch DIP facility, the Court noted that the priming DIP charge would not secure any obligations that were owing prior to the filing. However, in the CCAA Part 4 recognition proceedings of *Hartford Computer Hardware Inc., Re*, [33] it was expressly noted that a provision in the DIP agreement, which required that all cash collateral that comes in the possession of the debtor after the petition date would be deemed to have been remitted to the pre-petition lender for the repayment of the pre-petition credit facility, would *not* be permissible under section 11.2(1) of the CCAA.

With respect to creeping roll-ups, several courts have approved interim DIP financing facilities that required the applicants to use receipts from operations to pay down pre-filing obligations. [34] In *Angiotech*, the Court approved an initial order which directed the debtors to cash collateralize the pre-filing obligations, and that the DIP charge would not secure any obligations that were incurred pre-filing in accordance with section 11.2 of the CCAA. [35] In *Cow Harbour*, the Court expressly held that the features of creeping roll-up DIP financing are not prohibited by section 11.2(1). [36] In rejecting the argument of certain creditors that the arrangement (in which a pre-filing credit facility was being converted to a DIP facility) violated section 11.2(1), the Court gave the following rationale:

> In other words, [the creditors] complain that [the DIP lender] is bootstrapping itself. From a strict statutory interpretation perspective, that interpretation is incorrect because the interim financing security does not secure the previous indebtedness. The term sheet says that. And I approved the initial order on that basis. The super-priority secures only the interim financing and no more.
>
> From a practical perspective, however, the creditors complain that the [lender's] nonprime security is becoming primed security because as [the lender] gets its initial money order paid it turns around and lends that money to the debtor under the interim financing. That would be a strong argument, except that the debtor is using the interim money financing to pay for its ongoing operations such as payroll. The payments to [the lender] are coming out of cash-flow not interim financing. If there were little or no ongoing costs then the creditor's argument would be much stronger. Granted at this time there is no interim financing money outstanding, but we are all aware that the debtor had to meet payroll on April 9, 2010, using interim financing money, and I suspect it will have to meet it again on April 30, 2010. [37]

In the CCAA proceedings of *Comark*, [38] the Court approved a DIP financing facility which in essence provided for a creeping roll-up on the basis of an approval of the existing cash management system. In *Comark*, the cash management system in effect prior to the CCAA proceedings required that all cash be deposited into a blocked account, which was under the control of a pre-filing secured lender. In order for Comark to access liquidity in the CCAA proceedings, Comark was required to deposit all cash from operations into the blocked account in order to pay down the pre-filing revolver facility. Payments towards the pre-filing revolver would result in availability under the DIP facility extended by the same pre-filing secured lender. The Court accepted that, since the pre-filing revolver facility was only being reduced by the use of Comark's cash generated from its business, the DIP charge would only be securing advances made post-filing under the DIP facility. Accordingly, the DIP charge would not secure an obligation that existed prior to the commencement of the CCAA proceedings.

There has yet to be judicial consensus or a fully reasoned analysis as to the availability of roll-ups or creeping roll-ups. The authors argue that, subject to certain conditions and checks and balances being put in place to protect stakeholders, roll-ups should be permitted in certain circumstances. Roll-ups can protect a creditor with a first ranking security interest on all of a debtor's accounts receivable and inventory from being prejudiced by the erosion of its working capital collateral.

The issue with respect to the uncertainty of the use of roll-ups has arguably manifested as a result of the varying interpretations of section 11.2 of the CCAA. Section 11.2 of the CCAA provides that a DIP charge may not secure an obligation that exists before the order approving the DIP financing is made. [39] This section of the CCAA came into force with the 2009 amendments to address an issue that arose in the *Air Canada* [40] CCAA proceedings in which a DIP lender was able to secure its unsecured pre-filing aircraft lease obligations with the DIP charge, thereby directly elevating its pre-filing debt to super-priority secured indebtedness.

In order to address the risk of preferences and cross collateralization, a plain reading of section 11.2 of the CCAA results in a narrow restriction — that a DIP charge cannot secure a pre-filing obligation. This is consistent with the *White Birch* decision. There is nothing in the language that suggests that DIP financing, secured by a DIP charge, cannot be used to pay pre-filing obligations, including a pre-filing loan. Some insolvency practitioners would suggest that the payment of pre-filing obligations using DIP proceeds or cash from operations indirectly secures such pre-filing obligations in contravention of section 11.2 of the CCAA. If this interpretation were true, all payments of pre-filing obligations such as wages and critical supplier payments would be in contravention of section 11.2 of the CCAA. Accordingly, the authors contend that full or creeping roll-ups should be permitted if they are fully disclosed to the court and, if based on the circumstances of each case, they do not prejudice the rights of other stakeholders by altering their relative priorities.

Roll-up, or creeping roll-ups, are often necessary to protect pre-filing working capital lenders who become the DIP lender. Under a pre-filing loan, a lender advances funds on the strength or value of the debtor's assets, including its receivables and inventory. The logic is that, since the pre-filing working capital lender's loans were used to generate this working capital and, assuming its security is valid and enforceable, the pre-petition lender should be able to recover that collateral rather than have it dissipated or diminished by funding the proceedings. If the working capital lender lent based on asset-based lending formulas, it relied on the recovery of that very collateral for its repayment (not necessarily a going-concern sale). It is often the case that the level of working capital generated during the CCAA proceedings is reduced, thereby compromising the repayment of the pre-petition loan which was originally advanced based on its strength of such working capital. Accordingly, a roll-up or creeping roll-up seeks to mitigate this risk for a pre-filing lender. With respect to a DIP lender, the reduction in working capital doesn't present the same risk as new DIP loan advances are made with the full costs and impact of the restructuring proceedings taken into account when determining the amount of the DIP loan commitments and conditions of availability. DIP roll-ups may also permit more DIP loans in proceeding being offered by parties that are willing to refinance the existing lenders to avoid hostile DIP loan fights.

Courts should consider, approving full or partial roll-ups and continuing to approve creeping DIP roll-ups in appropriate circumstances where:

• the monitor has provided an opinion as to the validity and perfection of the pre-filing lender's security;

• the debtor can establish that the roll-up or creeping roll-up does not alter the relative priority of the claims of other creditors to the pre-filing working capital that will be used to repay the pre-petition loan or that appropriate protections for such priority claims have been developed;

• the DIP lender is not obtaining an undue advantage relative to other creditors;

• stakeholders are given adequate notice of the DIP approval motion which includes the roll-up or creeping roll-up provision so that stakeholders who may be prejudiced can oppose the use of the roll-up or creeping roll-up; and

• the availability of a mechanic which can reverse the roll-up in the event there is a successful challenge by other creditors as to the validity, enforceability, extent, perfection or priority of the pre-filing lender's claims.

7. NOTICE — NOT NECESSARILY ALWAYS BETTER LATE THAN NEVER

In approving DIP financing, section 11.2 of the CCAA requires a debtor to provide notice to affected secured creditors. While notice to affected secured creditors is essential because of the priming element of DIP financing, the authors take the view that adequate notice should be provided to all stakeholders as the terms of a DIP proposal, including pricing and control provisions, may be prejudicial to all stakeholders. Notice of a proposed legal action that could affect the rights of interested parties is a fundamental component of any just, fair and effective legal process. Adequate notice of an application for DIP financing provides stakeholders with a reasonable opportunity to consider the merits of the application, engage in informal negotiations and, if necessary, prepare responding materials.

In order to ensure that adequate notice is given to all stakeholders, and that stakeholders have an opportunity to come before the court to oppose the DIP financing, the courts have recently begun to limit the availability of DIP financing to the minimum amount necessary for the debtor to operate in the first week prior to the comeback hearing. The approval of the limited amount of financing ensures that a DIP is not a *fait accompli* before stakeholders have had time to consider the DIP and its impact.

The importance of adequate notice of an application for DIP financing was underscored in *White Birch* where insufficient notice to a major secured creditor led the Court to agree with the secured creditor's contention that it should be allowed to attend a *de novo* hearing where the whole issue of granting a DIP loan and corresponding super-priority would be heard again despite an earlier order of the Court granting super-priority DIP financing.[41] As the Court stated in *White Birch*, "the whole substance of the CCAA is based upon the principle of having and maintaining a 'level playing field' among the various stakeholders involved in a restructuring process".[42]

In the CCAA proceedings of *Indalex Ltd., Re*,[43] the Court was confronted by pension plan members who argued that the debtor's failure to give adequate notice of their motion for DIP financing prejudiced the plan members' ability to fully argue their position. In *Indalex*, the debtor company solicited terms from a variety of possible DIP lenders and eventually agreed to accept the DIP loan offered by a syndicate of pre-filing senior secured creditors. On April 8, 2009, the CCAA Court issued an amended initial order authorizing the debtor to borrow $24.4 million from the DIP lenders and to grant them security over all creditors. The Court found that the plan members did not participate in the initial proceedings and received little or no notice of the motion requesting DIP financing. The Supreme Court of Canada found that the plan administrator's duty to the plan members meant that, at the very least, the plan members were entitled to reasonable notice of the interim financing motion so that they could have the opportunity to present their arguments.[44]

In the United States, DIP financing is ordered on a split basis, with an interim order being granted on little or no notice and the balance being approved on a hearing for approval of a final DIP order, on 20 days notice to interested parties. The 20-day period provides ample opportunity for stakeholders to understand often complex drafted DIP financing proposals and how such proposals will impact them. In the recent Chapter 11 filing of Molycorp, Inc.,[45] the notice period provided the opportunity for the debtors to achieve more favourable DIP financing arrangement and maximize value for all stakeholders. In *Molycorp*, the debtor sought court approval of a total $135 million DIP by way of an interim order approving only $22 million with the balance to be approved pending a final DIP hearing 20 days later.[46] As a result of opposition to the proposed DIP, in the period between the granting of the interim order and the final order, the terms of the DIP financing were renegotiated to remove onerous terms such as a full roll-up of pre-petition debt and consent rights over the Chapter 11 plan. It is the authors' view that the comeback hearing required as part of the model initial order in Ontario should be, at least as it pertains to the DIP loan, extended from seven days to 20 days to allow impacted stakeholders with the necessary time to consider a DIP proposal and its terms.

In addition to the foregoing, to alleviate the time constraints and better enable a court and stakeholders to properly understand what are typically complex and cumbersome DIP agreements, a monitor's report should contain a concise statement of all of the material provisions in the DIP agreement, including control features, roll-ups, whether there is a determination of the validity of pre-filing security, milestones and deadlines to approve a transaction or a plan, the treatment of pre-filing debt, pricing and economic terms (including the dollar amount of required commitment fees and other costs, the payment of professional fees) and provisions which affect or limit the court's power or discretion.

8. CONCLUSION

It is the authors' view that DIP financing is alive and well in Canada, which is encouraging given that DIP financing is often critical for most CCAA debtors and can be a determinative factor in the success of any restructuring. The authors believe that discussion of these issues both outside and within the court, and the corresponding judicial determination by the court with respect to these issues, is healthy for our practice and for its evolution. This paper is an attempt to add to the ongoing dialogue.

Footnotes

* Waël Rostom is a partner at McMillan and Caitlin Fell is an associate at McMillan.

2 R.S.C. 1985, c. C-36 [CCAA].

3 R.S.C. 1985, c. B-3 [BIA]. This paper will focus exclusively on the CCAA.

4 See *United Used Auto & Truck Parts Ltd., Re*, 2000 BCCA 146, 2000 CarswellBC 414 (B.C. C.A.); leave to appeal allowed 2000 CarswellBC 2132, 2000 CarswellBC 2133 (S.C.C.); *T. Eaton Co., Re*, 1997 CarswellOnt 1914, 46 C.B.R. (3d) 293 (Ont. Gen. Div.); *Dylex Ltd., Re*, 1995 CarswellOnt 54, 31 C.B.R. (3d) 106 (Ont. Gen. Div. [Commercial List]).

5 CCAA, *supra* note 1, s. 11.2(1).

6 *Ibid.* s. 11.2(4).

7 *Canwest Publishing Inc./Publications Canwest Inc., Re*, 2010 ONSC 222, 2010 CarswellOnt 212 (Ont. S.C.J. [Commercial List]) at para. 45.

8 *Comark Inc., Re*, 2015 CarswellOnt 20810 (Ont. S.C.J.) [*Comark*].

9 *Crystallex International Corp., Re*, 2012 ONSC 2125, 2012 CarswellOnt 4577 (Ont. S.C.J. [Commercial List]); affirmed 2012 CarswellOnt 7329 (Ont. C.A.); additional reasons 2012 CarswellOnt 9479 (Ont. C.A.); leave to appeal refused 2012 CarswellOnt 11931, 2012 CarswellOnt 11932 (S.C.C.) [*Crystallex*].

10 *Ibid.* at paras. 88-90.

11 *Ibid.* at para. 91.

12 *Ibid.* at paras. 23, 28.

13 *Ibid.* at para. 89.

14 *Great Basin Gold Ltd., Re*, 2012 BCSC 1459, 2012 CarswellBC 2996 (B.C. S.C.) [*Great Basin*].

15 *In re Tenney Village Co., Inc.*, 104 B.R. 562 (Bktcy. D. N.H., 1989) at p. 568.

16 *Great Basin, supra* note 13 at para 181.

17 *Ibid.* at para 179.

18 *Essar Steel Algoma Inc.* (November 9, 2015), Doc. CV15-000011169-00CL (Ont. S.C.J.).

19 *Ibid.*

20 *Essar Steel Algoma Inc.* (November 9, 2015), Doc. CV15-000011169-00CL (Ont. S.C.J.) (Affidavit of Rajat Marwah) at para. 135.

21 *Essar Steel Algoma Inc.* (November 16, 2015), Doc. CV15-000011169-00CL (Ont. S.C.J.) (Endorsement of Newbould, J.).

22 *Ibid.* at para. 2.

23 *Ibid.* at para. 1.

24 *Ibid.* at para. 2.

25 *Essar Steel Algoma Inc.* (December 23, 2015), Doc. CV15-000011169-00CL (Ont. S.C.J.) (Applicants' Motion Record Exhibit 2B) at para. 30-31.

26 American Bankruptcy Institute, *Commission to Study the Reform of Chapter 11: Final Report and Recommendations* (Alexandria, VA: The Commission, 2014), online: <http://commission.abi.org/full-report>.

27 *Royal Bank v. Soundair Corp.*, 1991 CarswellOnt 205, 7 C.B.R. (3d) 1 (Ont. C.A.) [*Royal Bank*].

28 *Crystallex, supra* note 8.

29 *Royal Bank, supra* note 26.

30 *Crystallex, supra* note 8 at para. 19.

31 *Royal Bank, supra* note 26.

32 *White Birch Paper Holding Co., Re,* 2010 QCCS 1176, 2010 CarswellQue 2675 (C.S. Que.) [*White Birch*].

33 *Hartford Computer Hardware Inc., Re,* 2012 ONSC 964, 2012 CarswellOnt 2143 (Ont. S.C.J. [Commercial List]).

34 *Cow Harbour Construction Ltd., Re* (April 7, 2010), Doc. Bktcy. 24-115359 (Alta. Q.B.) at para. 51; *Angiotech Pharmaceuticals Inc., Re,* 2011 CarswellBC 124 (B.C. S.C. [In Chambers]) [*Angiotech*]; *Hart Stores Inc. / Magasins Hart inc., Re,* 2012 QCCS 1094, 2012 CarswellQue 2549 (C.S. Que.); *Catalyst Paper Corporation, Re* (January, 31 2012), Doc. S120712 (BC. S.C.).

35 *Angiotech, supra* note 33 at paras. 47 and 47A.

36 *Cow Harbour Construction Ltd., Re* (April 28, 2010), Doc. 1003 05560, EVQ10CO-WHARB (Alta. Q.B.).

37 *Ibid.*

38 *Comark, supra* note 7.

39 CCAA, *supra* note 1, s. 11.2(1).

40 *Air Canada, Re,* 2003 CarswellOnt 1220, [2003] O.J. No. 1157 (Ont. S.C.J. [Commercial List]).

41 *White Birch, supra* note 31 at para 26.

42 *Ibid.* at para. 9.

43 *Indalex Ltd., Re,* 2013 SCC 6, 2013 CarswellOnt 733, 2013 CarswellOnt 734 (S.C.C.).

44 *Ibid.* at para. 73.

45 *In re Molycorp, Inc., et al,* Bkcty. Delaware No. 15-11357.

46 Molycorp, News Release, "Molycorp, Inc. Receives Court Approval for $22 Million in Interim Financing to Support Operations" (3 July 2015).

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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 LAURENTIAN UNIVERSITY OF SUDBURY

Applicant

Court of Appeal File No. M52471
Superior Court File No.: CV-21-656040-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

Proceeding commenced at Toronto

BOOK OF AUTHORITIES OF THE MOVING PARTY
(Motion by Thorneloe University for leave to appeal)

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