CITATION: Waygar Capital Inc. v Quality Rugs of Canada Limited, 2024 ONSC 2486
COURT FILE NO.: CV-23-00703292-00CL
CV-23-00703933-00CL
DATE: 20240705

SUPERIOR COURT OF JUSTICE – ONTARIO

COMMERCIAL LIST

RE: WAYGAR CAPITAL INC., as agent for NINEPOINT CANADIAN SENIOR DEBT MASTER FUND L.P., Applicant

AND

QUALITY RUGS OF CANADA LIMITED, MALVERN CONTRACT INTERIORS LIMITED, WESTON HARDWOOD DESIGN CENTRE INC., ONTARIO FLOORING LTD., TIMELINE FLOORS INC., AND QUALITY COMMERCIAL CARPET CORPORATION, Respondents

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 WITH RESPECT TO QUALITY RUGS OF CANADA LIMITED AND OTHER COMPANIES.

BEFORE: Penny J.

COUNSEL: See attached participant list

HEARD: April 25, 2024

ENDORSEMENT

Overview

[1] The Quality Sterling group of companies ("QSG"), which is the subject of these proceedings, operates as a flooring contractor serving the residential and commercial construction markets. In August 2023, it was the largest flooring contractor in Canada, with operations in Ontario, Alberta and British Columbia.

[2] QSG sought and was granted the protection of a stay, and other relief, under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36. A proposed transaction which might have preserved QSG as an ongoing business could not ultimately be concluded. A receiver was appointed on application by QSG's senior lender.

[3] These proceedings have affected the rights of various suppliers to QSG's many projects (the Suppliers). Enforcement of their prefiling lien and trust claims has been stayed. Since

the commencement of these insolvency proceedings, QSG (under the supervision of the Monitor) and then the Receiver, have paid for the continued supply of flooring material and installation services for QSG's projects on a cash on delivery basis.

[4] The Suppliers assert trust claims against QSG's accounts receivable; in Ontario, this is based on s. 8 of the *Construction Act*. However, as I will explain in more detail below, QSG, and then the Receiver, have found it necessary to use funds received through payment of accounts receivable to fund ongoing operations. Thus, funds that were otherwise potentially impressed with a statutory trust have been used during the CCAA and receivership proceedings to fund QSG's ongoing operations with a view to maximizing benefit for creditors generally.

[5] In this context, the Suppliers sought what was styled a "Lien and Trust Regularization Order" ("LTRO") that would recognize their trust rights and cure the substantive prejudice caused by the court-ordered stays. They sought an order:

> (a) declaring that all funds owing to or received by QSG on account of the contract or subcontract price of an improvement constitute a trust fund for the benefit of Suppliers with a proven trust claim;
>
> (b) granting super-priority trust and lien charges (TLC) over all of the QSG's property to secure all amounts owing in respect of a:
>
> > (i) a lien claim proven through the claims process to the extent of any applicable holdback; and
> >
> > (ii) any trust claim that would have constituted a proven trust claim as of August 4, 2023, to the extent that QSG converted trust funds over the course of the CCAA proceeding; and
>
> (c) ordering that the trust fund and TLCs are subject to the Administration Charge and Receiver's Charge previously granted in these proceedings, but rank in priority to all other security interests, including the DIP Lender's Charge which was also previously granted in these proceedings.

[6] In an endorsement of December 7, 2023, I granted the Suppliers' request for an order creating the TLC over the Suppliers' proven trust and lien claims. No one seriously opposed this relief, in concept at least. On the question of the relative priority of the TLC in relation to several other existing charges granted under prior orders of this court (that is, a DIP Lender's Charge, a Financial Advisor's Charge and a D&O Charge), there was significant controversy. This controversy involved the relationship between orders made by the Superior Court of Justice under the CCAA and rights under provincial legislation such as s. 8 of the *Construction Act*, and ultimately, the application of the doctrine of federal paramountcy.

[7] I requested additional submissions on this point. These were received in January 2024. This lead to a further motion, under Rule 59.06(1) of the Rules of Civil Procedure, by the DIP Lender (Ironbridge), the Financial Advisor (Alvarez) and the directors and officers of the

Quality Sterling Group (D&Os) to vary the language of the Initial Order and the ARIO. This motion was argued on April 24, 2024.

[8] These reasons, therefore, deal both with the April 24, 2024 motion to vary and the relative priorities issue still outstanding from the Suppliers' December 7, 2023 motion.

[9] For reasons I will explain below, the motion to vary the Initial Order and the ARIO is granted. The Suppliers' motion for an order ranking the TLC priority ahead of the DIP Lender's Charge, the Financial Advisor's Charge and the D&Os Charge is dismissed. In the unique circumstances of this case, the TLC shall have a super-priority charge over all charges and debts *other than*: the Administration and the Receiver's Charge; the DIP Lender's Charge; the Financial Advisor's Charge; and the D&O Charge.[1]

Background

CCAA and Receivership Proceedings

[10] QSG's primary lender was Waygar Capital Inc, as agent for Ninepoint Canadian Senior Debt Master Fund LP. Waygar provided QSG with a revolving working capital loan on a borrowing base calculation prescribed in the credit agreement. As of August 1, 2023 the outstanding indebtedness was over $50 million. It is important, for the purpose of these particular motions, that the Waygar credit agreement specifically excludes the holdback and trust funds that are the subject of the proposed TLC from the borrowing base.

[11] On August 3, 2023, Waygar and QSG brought competing CCAA applications, and Waygar brought a back-up receivership application, all in respect of QSG. It is also important for this motion that, on the same day, relying on enforcement provisions in its credit agreement, Waygar "swept" available cash in certain bank accounts held by QSG. The cash taken by Waygar from QSG's accounts involved about $6 million.

[12] On August 4, 2023, I granted QSG a stay of proceedings to provide QSG and Waygar with time to either litigate or negotiate a resolution. After successful negotiations, QSG, Waygar, Ironbridge Equity Partners IV, LP and Ironbridge Equity Partners (International) IV, LP (the "DIP Lender" or "Ironbridge") agreed that the DIP Lender would advance funds to facilitate the CCAA proceeding in connection with a bid by Ironbridge to purchase the assets of QSG (the "Proposed Transaction"). The purchase price for the Proposed Transaction included a cash component with QSG funding its operations through the CCAA proceedings from two sources: a $5 million DIP loan and QSG's accounts

---

[1] I should emphasize that the result in this case was driven by the "unique circumstances" of this case which include the timing and manner in which the Suppliers' arguments were raised. The circumstances giving rise to the Suppliers particular conundrum are not commonly faced in CCAA or other insolvency proceedings. This is because is it more often the owner or developer, rather than a contractor a form of "middleman"), who is the applicant seeking protection from their creditors. By concluding that an operational conflict exists in this case by virtue of the Charges granted by the court on August 25 and September 5, 2023, I am not saying anything about whether, had the full weight of the Suppliers' substantive arguments been made at or before the comeback hearing considering approval of the DIP and other Charges, those Charges would have been granted at all, or in the form that they were. That issue must be left for another day, to be argued on other facts and circumstances.

receivable. If the accounts receivable of QSG were not available to pay the obligations of QSG as they generally became due during the CCAA proceedings, the DIP financing required would have been well in excess of $10 million.

[13] On August 25, 2023, I granted QSG an Initial Order under the CCAA:

(a) continuing the stay of proceedings and providing other customary protections under the CCAA;

(b) appointing RSM Canada Limited as Monitor;

(c) staying the rights of suppliers of services and/or materials to QSG, including the Suppliers, from seeking to preserve, perfect or otherwise enforce any lien claim available to them in accordance with the usual protocols under applicable provincial lien legislation, including the *Construction Act*, and requiring that they instead deliver a notice of such lien claim to the Monitor;

(d) ordering a super-priority charge over all of the property of QSG, including:

> (i) a lien charge in respect of all lien claims proven in the CCAA proceeding; and
>
> (ii) a DIP Lender's Charge in connection with a debtor-in-possession facility from the DIP Lender to fund QSG's day-to-day operations pending the completion of the Proposed Transaction, on the terms set out in the DIP facility loan agreement (the "DIP Loan").

[14] The Initial Order was amended and restated after a comeback hearing on September 5, 2023 (the "ARIO"). The ARIO, among other things:

(a) continued the stay with respect to the enforcement of lien rights set out in the Initial Order;

(b) ordered that any lien claim that had been preserved by registration against the owner's property be vacated and deemed the claimant to have filed a notice of their lien claim with the Monitor;

(c) ordered that any lien claimant who delivered a timely notice of its lien claim was deemed to have preserved and perfected its lien for the purpose of provincial lien legislation;

(d) removed the lien charge as a super-priority charge (it was always contemplated that this would be replaced with a lien regularization order ("LRO") to be negotiated); and

(e) confirmed revised super-priority charges granted under the Initial Order in the following amounts:

> First – the DIP Lender's Charge but only to the extent of the assets in the Borrower's Account at any time from time to time;

Second – the Administration Charge (to a maximum amount of $750,000);

Third – the Directors' Charge (to a maximum amount of $600,000);

Fourth – the DIP Lender's Charge (to a maximum of $7,000,000 – this represented two tranches, an initial $5 million, and a possible additional $2 million); and

Fifth – the Financial Advisor's Charge (to a maximum of $950,000).

[15] By September 23, 2023, the entire initial $5 million DIP facility had been drawn down. The preconditions for the advance of the additional $2 million of DIP financing were never met. This left QSG's accounts receivable as the only source of QSG's operating funds.

[16] The plan for restructuring QSG under the CCAA revolved around the successful completion of the Proposed Transaction. On October 30, 2023, the DIP Lender informed the Monitor that it was not prepared to proceed with the Proposed Transaction. At this point, there was no resolution of the still to be negotiated lien regularization order.

[17] The Waygar receivership application was reinstituted. On October 31, 2023, I appointed Fuller Landau LLP as receiver and manager of the property, assets and undertakings of QSG.

[18] It is recognized by all stakeholders (and not in dispute) that QSG's only material asset is its accounts receivable. It has also been recognized since at least the inception of the receivership that, in construction projects such as the ones involved here, developers are reluctant to pay accounts receivable if the ability of a contractor to complete and warrant its work is in doubt. The Receiver has recognized (it is again common ground) that in the absence of any additional "new" money (which was not forthcoming after the termination of the Proposed Transaction), the Receiver would need to use existing accounts receivable, as they are paid, to finance QSG's ongoing operations and the ongoing receivership including realizing on the balance of QSG's main asset, its accounts receivable.

Issues

[19] There are two inter-related issues raised by the parties' arguments advanced in the Suppliers' motion for a super-priority:

(1) should the motions by the DIP Lender, the Financial Advisor and the D&Os to vary the Initial Order and the ARIO be granted; and

(2) assuming the Initial Order and ARIO *purport* to establish a super priority over provincial statutory trusts, is that super-priority valid and operative in the face of rights created by provincial statutory trusts?

[20] As these two issues are interwoven, I will address them together, more or less following the chronological events which gave rise to them.

Background and Legal Framework of the Issues and Arguments

[21] Insolvency law relies on provincial property law because the proprietary and contractual rights that are regulated by the bankruptcy process are usually created by virtue of provincial law. The *Construction Act*, for example, acts as one source of these proprietary and contractual rights by instituting a regime of liens, holdbacks and trusts. It is well established that the property rights created by the *Construction Act* are, on their face, constitutionally valid and do not operationally conflict with the BIA or the CCAA: *The Guarantee Company of North America v Royal Bank of Canada*, 2019 ONCA 9 at para. 3; *Re Urbancorp Cumberland 2 GP Inc*, 2020 ONCA 197 at paras. 33 and 34. This is, in essence, because s. 8(1) is not in pith and substance legislation in relation to bankruptcy. Rather, the priority-creating effects of s. 8(1) are purely incidental to a broader purpose of the legislation to "protect the rights and interests of those engaged in the construction industry and to avoid the unjust enrichment of those higher up the construction pyramid". The s. 8(1) trust was therefore the proper subject-matter of provincial legislation: *GCNA*, at paras. 30 and 32.

[22] Sections 7-13 of the *Construction Act* protect the interests of subcontractors and suppliers by impressing funds owing to or received by those to whom they have supplied their services or materials with a trust. Section 8 of the *Construction Act* provides that:

> 8(1) All amounts,
>
> a) owing to a contractor or subcontractor, whether or not due or payable; or
>
> (b) received by a contractor or subcontractor,
>
> on account of the contract or subcontract price of an improvement constitute a trust fund for the benefit of the subcontractors and other persons who have supplied services or materials to the improvement who are owed amounts by the contractor or subcontractor.
>
> (2) The contractor or subcontractor is the trustee of the trust fund created by subsection (1) and the contractor or subcontractor shall not appropriate or convert any part of the fund to the contractor's or subcontractor's own use or to any use inconsistent with the trust until all subcontractors and other persons who supply services or materials to the improvement are paid all amounts related to the improvement owed to them by the contractor or subcontractor.

[23] There are four elements required to establish a s. 8 trust, each of which the Suppliers say they will likely satisfy in the claims process. Suppliers must establish that:

(a) QSG is a contractor or subcontractor;

(b) the Suppliers supplied services or materials to projects on which QSG is a contractor or subcontractor;

(c) QSG has received or is owed monies on account of its contract price for those projects; and

(d) QSG owes money to the Suppliers for the services or materials supplied in respect of those projects.

[24] During the stay period QSG (and then the Receiver) used recovery of accounts receivable to fund operational expenses. This had the effect of depriving Suppliers of substantive property rights because trust funds were used up such that they are no longer traceable and lien rights have expired. The negotiated LRO never materialized during the CCAA proceedings and the receivership order ended the possibility of an LRO. It was in these circumstances that the Suppliers sought the TLC. And it was, essentially, on this basis that, subject to the dispute over the priority of the TLC in relation to the existing court-ordered super-priorities under the CCAA, no stakeholder opposed, and the court granted, the TLC.

Whether the TLC Should be Given Priority over the Existing Court-Ordered Charges

[25] The Suppliers submit that the TLC should rank ahead of all other charges against the property of QSG except for the Administration Charge and Receiver's Charge. This is because the receivables covered by the s. 8 trust and holdback regime are not the property of QSG. QSG's use of the trust funds was just as critical to QSG's operations as the DIP Financing. The trust funds made up the difference between the amount of DIP financing that Ironbridge was willing to advance, and the further funding required to continue operations which Ironbridge was not willing to advance. To the extent that Suppliers are able to establish that the now dissipated accounts receivable were subject to s. 8 trusts, QSG's use of the trust funds as supplementary operational funding forced the Suppliers to be involuntary DIP lenders. But for the interference with the Suppliers' rights, QSG would not have had access to this property. Parties were aware of and had the opportunity to structure their affairs having regard to the Suppliers' trust rights. Amounts for work done on projects which were held by or owed to a contractor in the circumstances were trust funds and consequently could not the property of the contractor until after all Suppliers had been paid. Accordingly, no security interests from lenders can attach to this property. Specifically, the Suppliers argue that Ironbridge knew or ought to have known that its security could not attach to trust funds under s. 8 and, to the extent that it did, this was an issue on which the Suppliers had reserved their rights. At the time of its DIP loan advances, Ironbridge knew or ought to have known about the potential impact the Suppliers' claims to trust funds and priority could have on its security.

<u>Analysis</u>

[26] To the extent the Suppliers argue that s. 8 trusts necessarily trump super-priorities granted under s. 11.2 of the CCAA, I am unable to accept their argument. While it is true that s. 8 trusts survive insolvency proceedings, it is equally clear that priorities created by provincial legislation may conflict with the court-ordered priority of a DIP charge under section 11.2. In that circumstance, there is an operational conflict and the court-ordered priority under the CCAA prevails to the extent of the conflict.

[27] In *Sun Indalex Finance, LLC v. United Steelworkers,* 2013 SCC 6, the Supreme Court unanimously concluded that a DIP charge supersedes a provincial statutory trust based on the doctrine of federal paramountcy: paras. 55-60. As in *Indalex*, here QSG would not have been able to engage in any restructuring efforts without DIP financing. In granting the DIP Charge, I concluded, among other things, that the CCAA's purpose would be frustrated without the DIP Charge because the Applicants could not progress with any restructuring efforts without additional funds, which would not be forthcoming without a super-priority charge to protect "new money" advances.

[28] Similarly, in *Comstock*, the debtor required DIP financing to continue its operations during its restructuring process and the DIP lender would not have advanced funds without the super-priority given by its DIP charge. Justice Morawetz (as he then was) concluded that it was appropriate for the DIP charge to take priority over the construction lien and trust claimants. In doing so, the Chief Justice accepted the reasoning of the applicants in that case that "*Indalex* is the correct resolution of the priority issue on the grounds of paramountcy in circumstances where, but for the granting of priority over a statutory deemed trust in favour of the DIP lender, the DIP financing would not be advanced and the distressed companies and its stakeholders would see an immediate halt to the restructuring": *Comstock Canada Ltd. (Re)*, 2013 ONSC 475 at para. 54.

[29] Finally, In *Urbancorp*, Justice Zarnett, writing for a unanimous panel, discussed the relative priority of statutory trusts arising under the former *Construction Lien Act*. While a statutory trust under provincial law may remain effective in an insolvency, it may not be effective if doing so would conflict with an order under the CCAA establishing a specific superior priority. This is because paramountcy would require that the trust be considered inoperative, in whole or in part, to the extent of the conflict: *Urbancorp,* at para. 45.

[30] In the present case, the Suppliers rely on *Urbancorp* (and *GCNA*) as support for the proposition that "property rights created by the *Construction Act* are constitutionally valid and do not operationally conflict with the BIA or the CCAA". As noted earlier, I agree with the Suppliers that the two statutes do not conflict on their face, and do not necessarily give rise to any operational conflict. However, the unanimous court in *Urbancorp* went on to conclude, based in part on the Supreme Court's decision in *Indalex*, that "a provincial trust can lose its effect under the CCAA to the extent the doctrine of paramountcy requires that result". In reaching this conclusion, Justice Zarnett explained that "charges may be created under the CCAA which, as a matter of paramountcy, will take priority over a provincial statutory trust". More particularly, "paramountcy renders the provincial trust inoperative only to the extent required to deal with the conflict, that is, by yielding priority to the DIP Financing Charge. The trust does not become wholly inoperative": *Urbancorp,* at para. 70.[2]

---

[2] The factum of Ames Tile and Stone Ltd. supported the submissions made by the Ontario Suppliers in general and focused on the specific provisions of the Alberta and B.C. legislation. While there are differences, especially between s. 8 of the *Construction Act* and the Alberta regime. I am not convinced that these differences change the essential point. The CCAA court has the authority to order super-priority charges and, when such priorities charges

[31] Ironbridge, Alvarez and the D&Os argue that this is exactly their situation. The Charges were required to give effect to the purposes of the CCAA. They created stability and ensured that funds for the necessary contributions of the professionals, financiers and the D&Os were protected. Without the Charges, there could be no restructuring and recovery of accounts receivable would be impaired. The Orders issued under the federal CCAA, to the extent they primed s. 8 rights under the provincial *Construction Act*, created an operational conflict to which the doctrine of paramountcy applied.

[32] It was in the context of the parties joining issue on this point that the specific language of the Initial Order and the ARIO became the focus of competing submissions before the court. Was there in fact an operational conflict? In their reply factum on the original December 7, 2023 motion, the Suppliers raised, for the first time, the argument that the relevant provision of the Initial Order (dated August 25, 2023, para. 47) and the ARIO (dated September 5, 2023, para. 47) did not purport to prime trusts at all, because the Model Order language respecting super-priority over "trusts" was deleted from those Orders. The Suppliers took the position that because the court's Orders made under the CCAA did not purport to grant express priority to the Charges over the Suppliers' trust claims (as distinct from the standard language of the Model Order), there was no operational conflict.

[33] It was this dispute, and the manner in which it arose, which gave rise to my order seeking further submissions on this point and, ultimately, to the motions brought by Ironbridge. Alvarez and the D&Os to amend or vary the Initial Order and ARIO under Rule 59.06 of the Rules of Civil Procedure. The Rule 59.06 motions were argued on April 24, 2024.

The Motion to Vary

[34] The Commercial List CCAA Initial Order Form provides, in para. 40, that various court-ordered charges shall rank in priority to all other security interests including, among other things, "trusts":

> THIS COURT ORDERS that each of the Directors' Charge, the Administration Charge and the DIP Lender's Charge (all as constituted and defined herein) shall constitute a charge on the Property and such Charges shall rank in priority to all other security interests, trusts, liens, charges and encumbrances, claims of secured creditors, statutory or otherwise (collectively, "Encumbrances") in favour of any Person.

[35] The Initial Order issued in this case, on August 25, 2023, and the ARIO issued on September 5, 2023, omitted the word "trusts" from the comparable paragraph (para. 47) in those Orders. The reason this happened was due to a mistake, the details of which are set out in the Monitor's Fifth Report. In that Report, the Monitor explains that:

- the QSG application took place in the context of competing CCAA applications by QSG and Waygar. It was "real time" litigation in which circumstance evolved and

conflict with those established by provincial legislation, the provincial priorities, while not invalid, are rendered inoperative to the extent of the conflict.

changed rapidly. The Monitor and its counsel became involved in the CCAA proceedings on August 1

- initially, it was assumed that there would be no request for DIP financing or a related charge. QSG had about $6 million in a blocked account which it expected to use to fund operations and professional fees during the CCAA proceedings. In para. 23 of its Report, the Monitor states:

  > As part of these amendments to the draft initial order, recognizing that QSG had approximately $6 million in its blocked account, mindful of the desire to be seen to be working with the suppliers, and recognizing that QSG would have to return later for approval of DIP financing, assuming that its application was successful, what is now paragraph 47 of the draft order was amended to (i) remove the word "trusts"; (ii) add the usual proviso protecting secured creditors who had not been served; and (iii) add language from paragraph 51 of the FirstOnSite Amended and Restated Initial Order regarding suppliers [the replacement of liens with a "lien charge" within the CCAA proceedings].

- prior to the service of the QSG CCAA application record, the draft initial order had not been shared with anyone other than QSG and the Monitor. These provisions were not the result of any negotiations or discussions with either Ironbridge or the Suppliers (who were not yet active in the case). Rather, this was a simple form of draft order prepared in the hope of the QSG application being successful on August 4, 2023, with the expectation that the $6 million would be available to QSG to fund operations. This form of draft initial order was intended to be merely a bridge to getting a firm deal with Ironbridge by the time of the comeback hearing

- on the afternoon of August 3, 2023, just prior to the first hearing on August 4, QSG and the Monitor learned that Waygar had "swept" from the blocked account all of the $6 million cash that QSG had planned to use for its post-filing operations. The expected availability of those funds had been a significant part of the decision to remove the word "trusts" from the draft CCAA initial order. However, throughout the negotiations which followed, no one ever picked up on the fact that the word "trusts" had been removed and that, in light of the changed circumstances (the "loss" of $6 million cash for use in operations and the now urgent need for DIP financing among them), it should be put back in the Initial Order and ARIO

- the competing applications were adjourned at the suggestion of the court on August 4 with a minimal stay and "status quo" order. Neither of the two CCAA applications was argued that day, and no one discussed or walked through any of the draft orders filed by either party in support of their applications

- negotiations between QSG, Waygar and Ironbridge ensued. Those negotiations were not completed by the August 18, 2023 return date. Accordingly, the terms of

the August 4th Order were extended to August 23, 2023. On August 23, 2023, the matter was again extended to August 25, 2023

- throughout this period, the focus was on the business terms of a possible DIP financing; very little time was spent considering or advancing the draft CCAA initial order that would be required in the absence agreement on the terms of a business deal

- discussions on open business and drafting points were still continuing after 1:00 AM on August 25. Details still remained to be ironed out by 10:00 AM, the appointed time for the hearing. The matter was stood down until 11:00. At 11:00 AM, a final deal was still not in place but limited submissions were made in the expectation that the proposed deal would be finalized shortly. The matter was again stood down until 12:30 PM

- the initial draft order was sent to the court and to the service list shortly after 1:00 PM. The hearing reconvened at 1:15. Counsel for the Monitor walked the court through the proposed draft order. There was no blackline from the Model Order; the removal of the word "trust" was not highlighted, was not brought to the attention of the court and was not discussed in any way. The draft order was issued in that form without, as it happened, the word "trusts" in para. 47

- at no point in any of the discussions or negotiations which the Monitor or its counsel had with either Ironbridge or QSG about the DIP term sheet was there ever a discussion or agreement that the DIP loan would not have priority over all manner of contractual or statutory security, liens or trusts. Those negotiations were indeed premised on the assumption that all of the Charges would have priority over statutory security, liens and trusts

- at that point in the proceedings, all of the beneficiaries of the Charges were aware that the principal source of recovery under any Charge would be from accounts receivable collections; the accounts receivable over which the Suppliers purported to claim a trust interest under s. 8. The word "trusts" should have been re-inserted but no one picked it up. There was, after August 4, no reason for that word to have been excised and the failure to re-insert it before August 25, 2023 was simply an oversight in the haste of dealing with the matter as it unfolded toward August 24 and 25, 2023

- at no point in the discussions regarding the form of the draft initial order were any of the Suppliers consulted on issues related to para. 47. There had been no prior involvement with any of the Suppliers on issues related to the priority of the Charges

- the oversight regarding the deletion of the word "trusts" from para. 47 continued throughout the ongoing proceedings, such that no one noticed the absence of the word "trusts" from para 47 before September 5, 2024, when the ARIO was issued with numerous amendments to the Initial Order (but no correction of the missing

"trusts" in para. 47). Indeed, it was not noticed until December 2023, when the Suppliers raised it in their reply factum on the Suppliers' motion for the TLC.

[36] The evidence from the DIP Lender, which has not been challenged, is that it agreed to provide the DIP Financing on the condition that it receive a super-priority charge over all of the property of QSG, including its accounts receivable. There was never a proposal raised, discussed, or agreed upon with the DIP Lender that would have seen the DIP Charge rank behind any lien or trust claims of the Suppliers. Had such a position been advanced, the DIP Lender would not have agreed to provide the DIP Financing before obtaining specific relief confirming the super-priority of the DIP Charge vis-à-vis any lien and trust claims. If that specific relief could not be obtained, the DIP Lenders would not have advanced the DIP Financing.

[37] The evidence of counsel to Ironbridge is that no one ever brought the deletion of the word "trusts" from the Model Order, or its absence from the Initial order or the ARIO, to their attention and they did not notice that it was missing. Nor were they ever privy to any discussion of why that word had been removed or the reasons for doing so. They saw no blackline to the Model Order or, if they did, the removal of the word "trusts" did not come to their attention.

[38] Similar evidence, also unchallenged, was advanced by Alvarez and by the D&Os.

[39] In short, on the evidence, the first time anyone noticed the absence of the word "trusts" from para. 47 of the Initial Order and the ARIO was when the Suppliers raised this point in their reply factum on the December 7, 2023 priority motion.

Rule 59.06

[40] Rule 59.06(1) provides a mechanism for varying any order of this court in two circumstances: first, where the order embodies "an accidental slip or omission"; and second, where the order requires amendment in any particular "on which the court did not adjudicate". The Rule provides:

> 59.06(1) An order that contains an error arising from an accidental slip or omission or requires amendment in any particular on which the court did not adjudicate may be amended on a motion in the proceeding.

The Arguments

[41] The moving parties submit that the deletion of the word "trusts" (and the inclusion of a closing proviso in each version of para. 47) was unequivocally the product of an "accidental slip or omission": first, by the Monitor and QSG (who without notice changed the language of the CCAA Orders and then failed to correct these changes when they should have done so); and, subsequently, by the DIP Lenders and other parties (who failed to notice and rectify these earlier errors, or at the very least, bring them to the parties, and the court's, attention).

[42] They also submit that because these errors were not immediately recognized, they failed to draw the salient parts of para. 47 to the attention of the court. Because the court was never made aware that the two CCAA Orders diverged from the standard provisions of the Model Order or what the reasons for that divergence were, the court never adjudicated upon either the appropriateness or the legal implications of these elements of the CCAA Orders.

[43] The moving parties also rely on the broad jurisdiction of the CCAA court under s. 11 to make any order that the court considers appropriate in the circumstances.

[44] The Suppliers argue that there was no slip or omission. The Applicants and the beneficiaries of the Charges put forward the order they wanted and it was endorsed by the court. They say the "intention" of the court was to issue the Initial Order and the ARIO in the form they were submitted. The fact that these orders diverged from the Model Order without explanation is not relevant because the Model Order is not binding on the court and should, in any event, be tailored to the circumstances of each case.

[45] The Suppliers also argue that the court did adjudicate on the issue of priorities when it issued the Initial Order and the ARIO. It granted a trust "carve out" from the typical super-priorities granted for charges of this kind due to the unique circumstances of this case. They also submit that this branch of the rule is limited to the rare case where the judge "forgot" to adjudicate on an issue that was raised at the hearing, which is not this case.

[46] The Suppliers argue, in any event, that the moving parties' conduct "disfavours" granting the remedy sought. They say that the moving parties' errors, though inadvertent, were objectively unreasonable. Each of the moving parties has provided evidence that the priority of their charge was critical to them, yet they failed to review, or appreciate, the language of the Orders in the thirty days between the Application Record being served and the return of the ARIO. Even if there was a failure of adjudication, the Suppliers point out that they would still be entitled to their day in court on the point. However, the priorities of their trusts are now moot because the passage of time and the difficulty of tracing payments from one owner to materials purchased for projects of other owners. The Suppliers' trust and lien remedies are realistically no longer available. The moving parties should not be allowed to retroactively create a paramountcy conflict when the Suppliers' position has already been prejudiced by the use of the trust funds over which they claim the TLC.

[47] Finally, the Suppliers argue that they detrimentally relied on the alleged "carve out" by not bringing forward the full panoply of their arguments to challenge the ARIO. This would have been on the basis that no charge should or could be granted on QSG's accounts receivable because they were subject to a trust and were, therefore, not QSG's property available to act as security against QSG's obligations to other creditors. The egg cannot be unscrambled. It cannot now be known what the court might have done at the comeback hearing had the Suppliers actively opposed the DIP and other Charges on this basis.

[48] On the issue of the discretion under s. 11, the Suppliers argue that the discretion granted under s. 11 must be used in a manner consistent with the purpose of the CCAA. There is

no restructuring purpose to retroactively granting the moving parties a priority over the construction trusts at this juncture in the proceeding.

[49] In addition, a variation under s. 11 would be, on the same basis as argued above, procedurally unfair. While efficiency and speed are important considerations under the CCAA, so are due process, respect for the interests of stakeholders and the important consideration that justice must be seen to be done through the observance of fair principles and processes.

Analysis

[50] The evidence clearly demonstrates that the sole source of the flaws in the Initial Order and the ARIO was a series of lapses by and miscommunications among counsel for the Monitor and the parties. The Rule 59.06 jurisprudence is replete with cases in which this court has exercised its remedial powers under Rule 59.06 to rectify errors and gaps in orders that are attributable exclusively to mistakes committed by parties or their counsel. Orders of the court should reflect the true intentions of the court. The court retains jurisdiction to amend an order where it does not reflect the court's intention.

[51] Here, the removal of the word "trusts" from para. 47 of the Orders was never specifically brought to my attention or the attention of the parties. I accept that this was due to the inadvertence of the Monitor and the parties and their counsel. I accept that the true intention of the relevant parties at the time was that the Charges, and in particular the DIP Charge, would have a priority over all other charges and obligations, including QSG's accounts receivable. This is clear from contemporaneous documents at the time, such as the term sheet which expressly provides that any advance of DIP financing by Ironbridge is conditional on a court-ordered super-priority charge over all the assets and undertaking of QSG, including accounts receivable. It is also consistent with the other "Charge" provisions of the two Orders.

[52] It was well known throughout these proceedings that QSG's accounts receivable were by far its most material asset. The DIP Financing provided to QSG was urgently needed. That financing allowed QSG to continue to operate and to pay ordinary course disbursements, including to the Suppliers, on a post-filing COD basis. Crucially, as I have found in the course of several other motions in these proceedings, the payment of ongoing ordinary course disbursements was key to advancing and completing projects and, thus, generating positive account receivable collections. Without the DIP Financing, QSG could not have continued in business and could not have realized on tens of millions of dollars of outstanding accounts receivable.

[53] The unchallenged evidence is that Ironbridge agreed to provide the DIP Financing on the condition that it receive a super-priority charge over all of the property of QSG, including its accounts receivable. There was never a proposal raised, discussed, or agreed upon with the DIP Lender that would have seen the DIP Charge rank behind any lien or trust claims of the Suppliers. Had any such position been raised, the DIP Lender unequivocally would not have agreed to provide the DIP Financing before obtaining specific relief expressly confirming the super-priority of the DIP Charge vis-à-vis any lien and trust claims. If that

specific relief could not be obtained, the DIP Lenders would not have advanced the DIP Financing.

[54] This was their *bona fide* understanding and, based on the evidence filed and submissions made to me at the time, it was my understanding as well.

[55] It was my intention, when the Initial Order and the ARIO were granted that, consistent with the Supreme Cout's observations in *Canada v. Canada North Group Inc*., 2021 SCC 30, *per* Cote J. at paras 30-31, the DIP Lender was to receive a super-priority charge over all the debtor's property, including, in this case, the all important QSG accounts receivable.

[56] I find, in the circumstances, that the errors which lead to the removal of the word "trusts" in para. 47 of the Orders constitute an accidental slip or omission within the meaning of Rule 59.06. I also find that these errors gave rise to a situation in which the issue now in dispute did not come to the court's attention and thus, was not subject to adjudication.

[57] In questions of this kind, the issues of prejudice, and relative prejudice, often arises and they do so here. Relief under Rule 59.06 may be denied if it would inflict genuine prejudice on one of the parties.

[58] The party claiming prejudice must provide evidence that it actually relied on the order to its detriment or did something on the strength of the order that would make it unfair to revisit the issue. Bald or purely speculative assertions of prejudice will not suffice. The court must investigate whether an opportunity has actually been foregone or whether a change in position has actually taken place in reliance on the order. The court must also consider whether refusing to grant an amendment will cause countervailing prejudice to the party that is seeking to rectify the order. The latter form of prejudice may "tip the balance" in favour of granting the requested amendment.

[59] The Suppliers contend that they "reasonably relied" on the existing ARIO and purportedly raised their current position with the Monitor and QSG on September 4, 2024. However, the Suppliers did not raise the position they now adopt with the DIP Lenders or the court at that time. The communication they rely on does not address the specific point now in contention at all. In fact, the Suppliers failed to raise this point at any time prior to delivering their reply factum for the December 2023 motion, four months after the ARIO, on December 5, 2024. To the extent that the Suppliers' supporting affidavits address reliance at all, they merely make bald statements that they "relied" on the provisions of the Initial Order and ARIO as approved, with no specific evidence of how they relied, or setting out facts establishing that the alleged reliance was in any way "detrimental" to their position in these proceedings. The Suppliers have not identified any genuine, legally cognizable prejudice that they will face if the requested amendments are made to correct the errors in the two Orders.

[60] The evidence supports the conclusion that the DIP Financing (which was not possible without the DIP Charge) provided a positive benefit to the Suppliers on many QSG projects. The Receiver reported that, from August to October 2023, almost $9 million was

paid to Suppliers on a COD basis. This was possible through a combination of paid accounts receivable and the $5 million made available by Ironbridge.

[61] I am unable to accept the Suppliers argument that they “lost the opportunity” to argue their position before the DIP Charge was approved. There is no evidence that the Suppliers were ready to make all these arguments but held off doing so in specific reliance on the absence of the word “trusts” in para. 47. The evidence is that, had these issues been raised, the DIP Lenders would have opposed. Had the Suppliers advanced these arguments and prevailed, no DIP Financing would have been advanced. Without the DIP Financing, the CCAA initiative would have failed and QSG would have been forced to liquidate, to the detriment of all stakeholders. Ongoing recovery of accounts receivable would have suffered.

[62] By contrast, failure to rectify the accidental slip or omission would give rise to significant prejudice to the DIP Lender, which advanced $5 million of “new” money, enhancing the possibility of a going concern transaction and, even more importantly as things turned out, enhancing the CCAA and post-CCAA receivership efforts to collect accounts receivable for the benefit of all stakeholders. The new money provided by Ironbridge benefited the process and, in doing so, benefited the Suppliers themselves. While less acute, the D&Os would also be prejudiced because they stayed on in their roles, relying on the protection of their Charge, and also enhanced ongoing operations and the collection of accounts receivable.

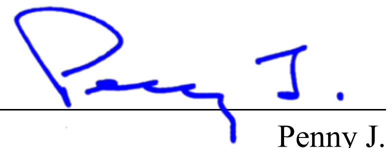
[63] Based on these findings, I conclude that the provisions of Rule 59.06 apply and that the relief sought in the moving parties’ notices of motion should be granted. III.

[64] Given my conclusion on the Rule 59.06 motion, I find it unnecessary to address the alternative argument regarding the general discretion of the court under s. 11 of the CCAA.

Conclusion

[65] For all these reasons, I grant the order sought by the moving parties in the Rule 59.06 motion. The Initial Order and the ARIO shall be amended and reissued in accordance with the grant of that relief. The Suppliers’ motion, to the extent of seeking a priority for the TLC ahead of the DIP Charge, the Directors; Charge and the Financial Advisor’s Charge, is dismissed on the basis that, by virtue of federal paramountcy, the CCAA Orders prevail. I have already granted the Suppliers partial relief in my endorsement of December 11, 2023.

[66] Outstanding issues related to the implementation of the results of both my decision of December 11, 2023 and this decision shall be addressed at a case conference to be convened at the parties’ convenience when it becomes appropriate to do so.



Penny J.

Date: July 5, 2024

Service List

TO: Steven L. Graff
sgraff@airdberlis.com

Matilda Lici
mlici@airdberlis.com

Counsel for Waygar Capital Inc., as agent for Ninepoint Canadian Senior Debt Master Fund L.P.

Don Rogers
drogers@waygarcapital.com

Counsel for the Applicant

Chris Besant
cbesant@grllp.com

Counsel for certain Former Directors and Officers of QSG

Kenneth Kraft
kenneth.kraft@dentons.com

Sara-Ann Wilson
sara.wilson@dentons.com

Sarah Lam
sarah.lam@dentons.com

Counsel for The Fuller Landau Group Inc. in its capacity court-appointed receiver and manager of Quality Rugs of Canada Limited, et al.

Ken Pearl
kpearl@fullerllp.com

Court-appointed receiver and manager of Quality Rugs of Canada Limited, et al.

Natasha MacParland
nmacparland@dwpv.com

Joshua Kuretzky
jkuretzky@dwpv.com

Natalie Renner
nrenner@dwpv.com

Derek Rici
dricci@dwpv.com

Counsel for Ironbridge Equity Partners Management Limited

Bryan Tannenbaum
btannenbaum@tdbadvisory.ca

Arif Dhanani
adhanani@tdbadvisory.ca

Monitor in the CCAA proceedings of Quality Rugs of Canada Limited, et al.

Joe Latham
jlatham@goodmans.ca

Erik Axell
eaxell@goodmans.ca

R. Chadwick
rchadwick@goodmans.ca

Andrew Harmes
aharmes@goodmans.ca

Counsel for RSM Canada Limited, in its capacity as Monitor in the CCAA proceedings of Quality Rugs of Canada Limited, et al.

Marc Wasserman
mwasserman@osler.com

Tiffany Sun
tsun@osler.com

Counsel for Mohawk Carpet Distribution, Inc.

Andrea Lutsch
alutsch@lawsonlundell.com

Kelly Hannan
khannan@lawsonlundell.com

Counsel for Taiga Building Products Ltd

Danny Nunes
danny.nunes@dlapiper.com

Bruce Darlington
bruce.darlington@dlapiper.com

Howard Krupat
howard.krupat@dlapiper.com

Counsel for Macro-Universe Enterprises Ltd. dba Fuzion Flooring

Michael Farace
Michael.Farace@devrylaw.ca

Counsel for GG Eight Cumberland Inc.

Edward Park
edward.park@justice.gc.ca

Pat Confalone
Pat.confalone@justice.gc.ca

Kelly Smith Wayland
kelly.smithwayland@justice.gc.ca

Sandra Tsui
Sandra.Tsui@justice.gc.ca

Matthew Gottlieb
mgottlieb@lolg.ca

Andrew Winton
awinton@lolg.ca

Counsel for Alvarez & Marsal Canada Securities ULC.

Demetrios Yiokaris
dyiokaris@kmlaw.ca

James Harnum
jharnum@kmlaw.ca

Counsel for LIUNA Local 183

Sherrise Carey
insolvency.unit@ontario.ca

Marin Leci
mleci@blg.com

Myles Fish
mfish@blg.com

Counsel for Housing One 10th Avenue Corporation

Akhil Vohra
avohra@ogilvielaw.com

Counsel for Ames Tile & Stone Ltd.

Manav Singhla
msinghla@millerthomson.com

Tony Van Klink
tvanklink@millerthomson.com

Counsel for Vifloor Canada Ltd.

Pierre Champagne
pierre.champagne@gowlingwlg.com

Haddon Murray
haddon.murray@gowlingwlg.com

James Aston
James.Aston@gowlingwlg.com

Counsel for Torlys Inc; Metropolitan Hardwood Floors (Eastern) Inc.; Lauzon – Planchers De Bois Exclusifs Inc.; Ceratec Inc.; and Boa- Franc SENC/GP

Daniel Wright
dwright@rousseaumazzuca.com

Michael Mazzuca
Michael@RousseauMazzuca.com

Michael Mandarino
mmandarino@rousseaumazzuca.com

Counsel for the United Brotherhood of Carpenters and Joiners of America

Robert Calderwood
rcalderwood@dzlaw.com

Counsel for the Auberge on the Park Residences

Evan Cobb
evan.cobb@nortonrosefulbright.com

Counsel for Stone Tile International Inc.

Adam Buckwold
ar@buckwold.com

Tushar Sabharwal
tsabharwal@dakllp.com

Marco Drudi
mdrudi@dakllp.com

Counsel for Olympia Title International Inc.

Jim Combatti
jimc@metrofloors.com

Peter Viitre
pviitre@sotos.ca

Counsel for Juliet Neely

Gregory W. Bowden
gwb@lbnfirm.com

Counsel for Royal Bank of Canada

Ian Dunbar
ian.dunbar@mcinnescooper.com

Counsel for Quality Sterling Group Halifax

Derek Brett
dbb@burnsidelaw.net

Counsel for 4405967 NS Limited

Lyle Brookes
lbrookes@chandos.com

Jeff Shankman
jps@jpscounsel.com

Caitlin Steven
csteven@chandos.com

Counsel for Geranium

Geoffrey Cullwick
gcullwick@brazeauseller.com

Eric Dwyer
edwyer@brazeauseller.com

Counsel for CDS Distribution Inc.

Gerard Borean
gborean@parenteborean.com

Devon Goyo
dgoyo@parenteborean.com

Counsel for Ciot Creditor

General E-mail Inbox
AGC-PGC.Toronto-Tax-Fiscal@justice.gc.ca

Christopher J. Henderson
Christopher.Henderson@toronto.ca

Georgia Tanner
Georgia.Tanner@toronto.ca

litigation@scotiabank.com

corporateca@dllgroup.com

customerservice@cwbnationalleasing.com

Alan B. Dryer
adryer@shermanbrown.com

Counsel for Lake & Town Homes Inc., Mobilio Homes Ltd. and Residences at Sugar Wharf Ltd.

Maria DiPietro
Maria.DiPietro@Chubb.com

Jenny Chamat Paniagua
Jenny.Chamat@Chubb.com

Alison R. Manzer
amanzer@cassels.com

Monique Sassi
msassi@cassels.com

Holly Elich
helich@cassels.com

Counsel for Equityline Flooring GP Inc.

J. Scott Myers
jsm@myerslaw.ca

Counsel for 1463825 B.C. Ltd. (Timeline Purchaser)

Julian R. Porritt
jrp@veritaslaw.ca

Counsel for BHappy Enterprises Inc. and European Touch Hardwood Inc.

Scott Bender
scott@boxconceptsfood.com

Landlord (Surrey, B.C. Property)

Kevin P. Von Bargen
kevin.vonbargen@kvb-law.com

Counsel for Strathern Heights Investments Inc., Landlord (Vaughan, ON Property)

Derek Ricci
dricci@dwpv.com

Natalie Renner
nrenner@dwpv.com

Rui Gao
rgao@dwpv.com

Jacqueline Houston
jhouston@dwpv.com
Counsel for the DIP Lenders / Moving Parties