Court File No. CV-15-11192-00CL

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 SECTION 101 OF THE *COURTS OF JUSTICE ACT,*
R.S.O. 1990, C. C-43, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF VICTORIAN ORDER OF NURSES FOR CANADA, VICTORIAN ORDER OF NURSES FOR CANADA – EASTERN REGION AND VICTORIAN ORDER OF NURSES FOR CANADA – WESTERN REGION

Applicants

BOOK OF AUTHORITIES OF THE APPLICANTS/ RESPONDENTS TO MOTION (RETURNABLE AUGUST 30, 2016)

August 24, 2016

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TAB 1

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Case Name:

AbitibiBowater inc. (Arrangement relatif à)

IN THE MATTER OF THE PLAN OF COMPROMISE OR ARRANGEMENT OF:
ABITIBIBOWATER INC.
and
ABITIBI-CONSOLIDATED INC., BOWATER CANADIAN HOLDINGS INC., The other Petitioners listed on Schedules "A", "B" and "C",
Debtors/Petitioners
and
ERNST & YOUNG INC., Monitor
and
THE ROYAL TRUST COMPANY, Mise en cause

[2010] Q.J. No. 31186

2010 QCCS 4218

EYB 2010-179004

192 A.C.W.S. (3d) 294

2010 CarswellQue 9502

No.: 500-11-036133-094

Quebec Superior Court
District of Montreal

The Honourable Clément Gascon, J.S.C.

Heard: August 30 and 31, 2010.
Judgment: September 8, 2010.

(130 paras.)

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Motion for directions on the identity of the persons whose benefits under the Bowater Supplemental

Executive Retirement Plans (SERP) were secured by a letter of credit -- Only the members of the SERP who retired before December 31, 2003, and those who were Canadian and retired after December 31 were entitled to share in the proceeds of the letter of credit -- Motion granted in part.

Motion for directions on the identity of the persons whose benefits under the Bowater Supplemental Executive Retirement Plans (SERP) were secured by a letter of credit -- The SERP's purpose was to give supplemental retirement benefits to a limited number of executives in addition to the benefits payable from any registered pension plan of Bowater Canadian Forest Products Inc. (BCFPI) -- On May 1, 2009, as a result of their insolvent status and the issuance of the Initial Order, BCFPI advised the Royal Trust Company (RTC) that they had suspended the payments of all SERP benefits and would not renew the letter of credit securing those -- RTC replied that it would call for payment on the letter of credit that it held and suspended all SERP payments -- There was a dispute as to which members were entitled to share in the proceeds of this letter of credit and as to how the proceeds were to be distributed -- The Petitioners considered that the members who had not yet begun to receive pension benefits under the SERP on May 26, 2009, namely the active employees and the deferred vested members, should not be entitled to share in the proceeds of the letter of credit -- The other members disputed the interpretation of the relevant sections of the SERP proposed by the Petitioners and insist that no resolution of BCFPI Board of Directors ever approved the purported changes made to the protection given to them by the letter of credit -- HELD: Motion granted in part -- It was a reasonable interpretation of the relevant provisions of the SERP to suggest that the letter of credit covers benefits in payment to the retirees and their beneficiaries, and not the potential future payments to active employees and deferred vested employees -- Only the members of the SERP who retired before December 31, 2003, and those who were Canadian and retired after December 31 were entitled to share in the proceeds of the letter of credit -- The active employees and the deferred vested members listed were not entitled to receive monthly SERP payments from the proceeds of the letter of credit There was no requirement of a resolution for such an amendment to authorize officers to modify the SERP.

Statutes, Regulations and Rules Cited:

Companies' Creditors Arrangement Act

Counsel:

Me Stephen Hamilton and Me Michel Legendre, Attorneys for the Debtors/Petitioners.

Me Mason Poplaw and Me Isabelle Vendette, Attorneys for the Mise en cause, The Royal Trust Company.

Me Normand Perreault, Attorney for some of the members listed in Schedules A, B and C of the Motion.

Me Tina Hobday, Attorney for some of the members listed in Schedule C of the Motion.

Me Raymond Hébert, Attorney for some of the members listed in Schedules D and E of the Motion.

JUDGMENT ON RE-MENDED MOTION FOR DIRECTIONS ON THE IDENTITY OF THE PERSONS WHOSE BENEFITS UNDER THE BOWATER SUPPLEMENTAL EXECUTIVE RETIREMENT PLANS WERE SECURED BY A LETTER OF CREDIT (#677)

INTRODUCTION

1 [1] On April 17, 2009, the Court issued an order (as subsequently amended and restated, the "**Initial Order**") pursuant to the *Companies' Creditors Arrangement Act* (the "***CCAA***") in respect of (i) Abitibi-Consolidated Inc. ("**ACI**") and subsidiaries thereof (collectively, the "**Abitibi Petitioners**"), (ii) Bowater Canadian Holdings Inc. and affiliates and subsidiaries thereof (collectively, the "**Bowater Petitioners**") and (iii) certain partnerships.

2 [2] At that time, one of the Bowater Petitioners, Bowater Canadian Forest Products Inc. ("**BCFPI**"), was the sponsor of three Supplemental Executive Retirement Plans (the "**SERPs**"). The SERPs' purpose was to give supplemental retirement benefits to a limited number of executives in addition to the benefits payable from any registered pension plan of BCFPI. The SERPs provided these post-retirement benefits to various members, be they eligible employees or beneficiaries of deceased participants.

3 [3] Pursuant to a trust agreement (the "**Trust Agreement**"), the benefits payable under the SERPs were partially secured by a letter of credit held by The Royal Trust Company ("**RTC**"), in trust for the eligible members.

4 [4] On May 1, 2009, as a result of their insolvent status and the issuance of the Initial Order, the Petitioners advised RTC that they had suspended the payments of all SERPs benefits and would not renew the letter of credit securing those[1].

5 [5] On May 26, 2009, RTC replied that it would call for payment on the letter of credit that it held[2]. It did so on that day and thus received an amount of some $23,065,000[3].

6 [6] When this letter of credit was called for payment, there were, from a practical standpoint, five different categories of SERPs members:

a) 48 Canadian resident members who had retired before December 31, 2003;
b) 6 Canadian resident members who had retired after December 31, 2003 but

before May 26, 2009;

c) 3 U.S. resident members who had retired before December 31, 2003;
d) 11 members who were still active employees of BCFPI; and
e) 6 members who were deferred vested members, that is, terminated employees who had not yet begun to receive their pension benefits under the SERPs.

7 [7] Of these five categories, only the first three were being paid pension benefits under the SERPs when BCFPI advised RTC that it was suspending all SERPs payments.

8 [8] There is a dispute as to which members are entitled to share in the proceeds of this letter of credit and as to how the proceeds are to be distributed. By their Motion[4], the Petitioners seek a declaration that:

a) the only persons entitled to continue to receive monthly SERPs payments from the proceeds of the letter of credit held by RTC are:

i) The Canadian resident members of the SERPs who retired before December 31, 2003 (listed in Schedule A to the Motion);
ii) The Canadian resident members of the SERPs who retired after December 31, 2003 but before May 26, 2009, including Mr. Donald Campbell (listed in Schedule B to the Motion), but only on the value of their SERPs benefits accrued up to December 31, 2003; and
iii) The U.S. resident members of the SERPs, including Mr. Jerry Soderberg (listed in Schedule C to the Motion);

b) RTC should pay the full monthly SERPs payments to the persons entitled to receive such from the proceeds of the letter of credit until they are exhausted in accordance with Schedule F to the Motion or until further order of the Court.

9 [9] In short, the Petitioners consider that the members who had not yet begun to receive pension benefits under the SERPs on May 26, 2009, namely the active employees (listed in Schedule D to the Motion) and the deferred vested members (listed in Schedule E to the Motion), should not be entitled to share in the proceeds of the letter of credit.

10 [10] The Petitioners so conclude based upon the wording of the relevant sections of the SERPs, their interpretation and application of their terms, and the letters and notices they sent over the years to the SERPs members in relation to the meaning and intent of the protection afforded by

this letter of credit.

11 [11] Of course, the members listed in Schedules A, B and C to the Motion support the conclusions sought. Without surprise, the members listed in Schedules D and E, that the Petitioners consider must be excluded from any sharing, contest the Petitioners' position. They dispute the interpretation of the relevant sections of the SERPs proposed by the Petitioners and insist that no resolution of BCFPI Board of Directors ever approved the purported changes made to the protection given to them by the letter of credit.

12 [12] Through their Motion, the Petitioners also ask the Court to authorize BCFPI to amend the Trust Agreement in accordance with Amendment no 1 (the "**Amended Trust Agreement**")[5]. Amongst others, the Petitioners want to dissociate BCFPI from all of its obligations under the Trust Agreement and to create a committee of beneficiaries who would take over from BCFPI the power to give directions to RTC and to make all decisions regarding the funds still to be managed.

13 [13] RTC disagrees with most of the amendments proposed to the Trust Agreement. It does not want to dissociate BCFPI from the Trust Agreement and to be forced to deal from now on with a committee of beneficiaries, on terms and conditions that it finds unacceptable.

THE ISSUES

14 [14] Two questions are at issue here: 1) Are the future SERPs benefits of the active employees and the deferred vested employees covered by the letter of credit? 2) Should the Court incorporate the changes to the Trust Agreement proposed by the Petitioners?

15 [15] To analyse the two questions, a review of the applicable SERPs, the letter of credit, the relevant changes made over the years to the SERPs and the most current actuarial valuations of the SERPs is necessary at the outset.

THE SERPs

16 [16] Bowater Pulp and Paper Canada Inc. ("**BPPC**"), formerly Avenor Inc., implemented the first of the SERPs effective July 16, 1993 (the "**1993 SERP**")[6]. On July 1, 1995, this 1993 SERP was restated into three SERPs (collectively, the "**1995 SERPs**")[7]:

a) The Supplemental Retirement Benefit Plan for Grade 11 and under Employees of Bowater Pulp and Paper Canada Inc.;
b) The Supplemental Retirement Benefit Plan for Grade 12 and under Employees of Bowater Pulp and Paper Canada Inc.; and
c) The Senior Executive Retirement Plan.

17 [17] The rules of the 1995 SERPs were afterwards restated in 1997 (collectively, the "**1997 SERPs**")[8].

18 [18] Finally, effective January 1, 2002, BPPC and BCFPI merged and continued their operations under the name of BCFPI. On the merger date, BCFPI became the sponsor of the 1997 SERPs which were renamed as follows (collectively, the "**2003 SERPs**")[9]:

a) The Supplemental Retirement Benefit Plan for Grade 27 and under Employees of Bowater Canadian Forest Products Inc.;
b) The Supplemental Retirement Benefit Plan for Grade 28 and under Employees of Bowater Canadian Forest Products Inc.; and
c) The Senior Executive Retirement Plan of Bowater Canadian Forest Products Inc.

19 [19] Throughout the years, each of the 1995 SERPs, the 1997 SERPs and the 2003 SERPs have included the following provisions dealing with BPPC or BCFPI contributions and the letter of credit, the SERPs' interpretation and administration, and BPPC or BCFPI authority to amend the SERPs:

SECTION 4- CONTRIBUTIONS

4.01 no contribution shall be required from a Participant in respect of benefits payable under this Supplemental Plan.

4.02 The benefits payable under this Supplemental Plan shall, unless decided otherwise by Avenor Inc. at its entire discretion, be payable by the Corporation out of its operating funds as they become due and the Corporation shall be under no obligation whatsoever to pay contributions in advance to fund such benefits.

4.03 Notwithstanding Subsection 4.02, the Corporation will arrange for the payment of benefits provided under the Supplemental Plan to be secured through a letter of credit from a financial institution.

13.08 INTERPRETATION

a) This provision of this Supplemental Plan shall be interpreted in accordance with the laws of the Province of Quebec and shall be binding upon and enure to the benefit of the Corporation and its successors and assigns.
b) Headings wherever used herein are for reference purposes only, and do not limit or extend the meaning of any of the provisions of this Supplemental Plan.

SECTION 14- ADMINISTRATION

14.01 The Corporation shall decide on all matters relating to the interpretation, administration and application of this Supplemental Plan, consistently with the text of the Supplemental Plan.

14.02 To facilitate any action required to be taken by the Corporation under the Supplemental Plan, the Board of Directors of the Corporation may, at its discretion, delegate the responsibility for administration of the Supplemental Plan to any person(s) appointed specifically for this purpose to act on behalf of the Corporation.

SECTION 15- FUTURE OF THE PLAN

15.01 Notwithstanding anything to the contrary herein, the Corporation reserves the right to make amendments to this Supplemental Plan. Any such amendment shall be communicated in writing by the Corporation to the Participants indicating the effective date of such amendment which, subject to Subsection 15.02 below, shall not precede the date that such communication is deemed to have been received by the Participants pursuant to Subsection 13.07 hereunder. Furthermore, the Corporation will not have the right to make such amendment only in respect of one or more Participants but such amendment shall have to be made in respect of all Participants, excluding those Participants who have already commenced to receive benefits hereunder.

15.02 When an amendment is made to this Supplemental Plan pursuant to Subsection 15.01 above as a result of a corresponding amendment to the Registered Plan, such amendment shall take effect as of the same effective date as applicable in respect of the corresponding amendment to the Registered Plan.

15.03 no amendment made to this Supplemental Plan by the Corporation pursuant to this Section 15 can have the effect of reducing the amount or value of the benefits accrued by the Participants under this Supplemental Plan prior to the effective date of such amendment.

(Emphasis added)

THE LETTER OF CREDIT

20 [20] As appears from this section 4.02, BPPC or BCFPI had the obligation to pay the benefits under the SERPs out of their operating funds, as the benefits became due. There were no contributions by the participants (section 4.01) and BPPC or BCFPI were under no obligation to pay contributions in advance to fund the benefits (section 4.02).

21 [21] Pursuant to section 4.03, BPPC or BCFPI were required, however, to establish a trust to hold documentary credits or letters of guarantee or investments to secure the payment of the benefits under the SERPs to the members.

22 [22] On August 14, 1996, BPPC entered into the Trust Agreement with Montreal Trust Company ("MTC") so that MTC would hold a letter of credit (initially in the amount of $30,000,000) to secure the payment of the benefits under the SERPs[10].

23 [23] The Board of Directors' resolution approving the Trust Agreement referred to "an amount sufficient to cover the current level of liabilities of the Corporation under the SERPs" and to the fact that the letter of guarantee would be drawable "in the event the Corporation does not meet payment obligations to participants under the SERPs"[11].

24 [24] The Trust Agreement provided that MTC was to hold the letter of credit until such time as the Corporation defaulted on the payment of the benefits under the SERPs. MTC was then to call the letter of credit, hold the proceeds in trust for all eligible members of the SERPs, and distribute the proceeds to them to the extent that they were sufficient for that purpose.

25 [25] MTC was bound by the terms of the SERPs and required to perform such duties imposed upon it pursuant to the Trust Agreement and each related SERPs. MTC was entitled to act on the instructions or written directions of the Corporation.

26 [26] Effective January 1, 2003, RTC replaced MTC as trustee of the Trust Agreement holding the letter of credit[12].

27 [27] The letter of credit was renewed annually at various face amounts determined by BCFPI until it was called for payment in May 2009, triggering the receipt by RTC of the amount of approximately $23,065,000[13].

28 [28] The rules of the Income Tax Act (Canada) (the "**ITA**"), applicable to "Retirement Compensation Arrangements", required RTC to then pay a refundable tax to the Canada Revenue Agency ("**CRA**") of 50% of the amount it received upon calling the letter of credit. In addition, the ITA requires that 50% of any income (interest, dividend or capital gain) realized by RTC on the assets held under the Trust Agreement be paid to the CRA as a refundable tax. These amounts will

be refunded by the CRA after the end of each calendar year during which RTC pays SERPs benefits to the eligible SERPs members.

29 [29] The balance of the proceeds is presently held by RTC in 30-day Government of Canada Treasury Bills.

THE CHANGES TO THE 2003 SERPS

30 [30] Since 2003, BCFPI issued three letters and notices to the members to advise them of purported changes to the SERPs that affected which members' benefits were secured by the letter of credit.

31 [31] On November 24, 2003, BCFPI first sent a letter to the then 38 active (i.e. not retired) SERPs members[14]. The last paragraph of the letter stated that only the benefits of retired SERPs members and only SERPs benefits accrued up to December 31, 2003 would be secured by a letter of credit from then on:

> "Please be advised that SERP benefits for service from January 1st, 2004 for all Canadian operations will not be secured by way of a letter of credit. DB SERP benefits for service up to December 31st, 2003 will continue to be secured that way for former BPPC employees working in Canada. For employees who have elected the DC plan, the DC SERP applicable to service from January 1st, 2003 is not secured by a letter of credit. This limitation of the use of a letter of credit does not affect the calculation of your total pension benefits."
>
> (Emphasis added)

32 [32] Even though some active members, including, for instance, Mr. Cayouette who testified at hearing, apparently disagreed with BCFPI position, none of them formally raised any kind of opposition to this letter.

33 [33] On May 27, 2005, BCFPI sent another notice to the then 33 active SERPs members to further clarify what had been said in the 2003 letter, namely that only the benefits of retired SERPs members and only SERPs benefits accrued up to December 31, 2003 would be secured by a letter of credit[15]:

> "**Notice to former BPPC employees eligible for Supplementary Pension benefits**
>
> The purpose of this notice is to clarify the status of the letter of credit that pertains to the members of the Bowater Canadian Forest Products Inc.

Supplemental Retirement Benefit Plan for Grade 27 and Under, the Supplemental Retirement Benefit Plan for Grade 28 and Over and the Senior Executive Retirement Plan, which provide benefits to former employees of Bowater Pulp and Paper Canada Inc.

(...)

During this year's annual renewal process for the letter of credit, the Company reviewed the methodology applied to the calculation of the letter of credit in light of the language quoted above. The Company determined that the letter of credit will be calculated based on the following methodology:

- The letter of credit will secure the payment of benefits to retirees and survivors who have started to receive their pension under the plans; it will not secure in advance the payment of benefits that may become payable sometime in the future to active employees or to terminated employees who are not yet in pay status (terminated vested participants).
- As you have been previously notified in the letter describing the pension re-design, the letter of credit will only secure benefits attributable to service accrued through December 31, 2003 or through December 31, 2002 for members who have elected to participate in the DC plan effective January 1, 2003.
- Further, the letter of credit will only secure the payment of benefits attributable to service that is accrued through December 31, 2003 or through December 31, 2002 for members who have elected to participate in the DC plan effective January 1, 2003, based upon the earnings determined as of December 31, 2003 and based on the early retirement provisions that would have applied if termination of employment or retirement had occurred on December 31, 2003 taking into account the maximum pension payable from the registered plan at pension commencement.
- The benefits to be secured by the letter of credit are to be calculated as though the plans were wound up and benefits settled on the valuation date for members in receipt of a pension on that date.

The Company is currently updating the letter of credit in accordance with the principles described above. The amount of the letter of credit will be recalculated

on a periodic basis.

The calculations applicable to the letter of credit do not affect the calculation of your individual pension benefits. Your future retirement benefits will continue to be computed in accordance with the plan provisions, regardless of the amount of, or method of calculation applicable to, the letter of credit. If you should have any questions, please contact Georges Cabana at [...]."

(Emphasis added)

34 [34] On May 30, 2005, a similar letter[16] was sent to seven SERPs members who were deferred vested members on that date. It stated:

"**Notice to former BPPC employees eligible for Supplementary Pension benefits**

The purpose of this notice is to clarify the status of the letter of credit that pertains to the members of the Bowater Canadian Forest Products Inc. Supplemental Retirement Benefit Plan for Grade 27 and Under, the Supplemental Retirement Benefit Plan for Grade 28 and Over and the Senior Executive Retirement Plan, which provide benefits to former employees of Bowater Pulp and Paper Canada Inc. (BPPC).

(...)

During this year's annual renewal process for the letter of credit, the Company reviewed the methodology applied to the calculation of the letter of credit in light of the language quoted above. The Company has determined that the letter of credit will secure the payment of benefits to retirees and survivors who have started to receive their pension under the plans. It will not secure in advance the payment of benefits that may become payable sometime in the future to active employees or to terminated employees who are not yet in pay status (terminated vested participants). The benefits to be secured by the letter of credit are to be calculated as though the plans were wound up and benefits settled on the valuation date for members in receipt of a pension on that date.

The Company is currently updating the letter of credit in accordance with the

> principles described above. The amount of the letter of credit will be recalculated on a periodic basis.
>
> The calculations applicable to the letter of credit do not affect the calculation of your individual pension benefits. Your future retirement benefits will continue to be computed in accordance with the plan provisions, regardless of the amount of, or method of calculation applicable to, the letter of credit. If you should have any questions, please contact Georges Cabana at [...]."
>
> (Emphasis added)

35 [35] None of the active or deferred vested members apparently reacted to the letters or notices sent in 2005. Even if Mr. Cayouette testified that he did not remember reading the e-mail that was then allegedly sent to him as active employee, no one seriously disputes that these letters and notices were in fact duly sent by BCFPI. The Contestation filed by the members listed in Schedules D and E indeed appeared to accept the existence of these letters and notices. On the balance of probabilities, the Court finds that they were remitted to the members concerned by BCFPI.

36 [36] Subsequently, around September 2005, BCFPI requested that restatements of the SERPs be prepared effective as of January 1, 2003, including amendments that would reflect the content of the 2003 letters and the 2005 letters (the "**2003 Draft Restatement**").

37 [37] The 2003 Draft Restatement thus amended sections 1.02 and 4.03 of the BCFPI SERPs as follows[17]:

> "1.02 The restated text of this Supplemental Plan is effective as of January 1, 2003 and as of such date replaces and cancels the application of any prior plan or agreement, whether oral or written, between a participant therein and the Corporation and providing for supplemental retirement benefits to be paid to such participant in addition to those payable from any registered pension plan of the Corporation. However, this Supplemental Plan shall not apply to or otherwise modify benefits payable or the terms and conditions for payment of such benefits to any former employee who has retired from or otherwise terminated his employment with Bowater Canadian Forest Products Inc. or its predecessors or their affiliates prior to the effective date of this Supplemental Plan.
>
> 4.03 Notwithstanding Subsection 4.02, the Corporation will arrange for the payment of benefits provided under the Supplemental Plan to be secured through a letter of credit from a financial institution. <u>For greater certainty, such letter of credit shall not apply during active employment with the Corporation and shall</u>

> only apply from pension commencement. Furthermore, the letter of credit shall only apply in respect of benefits provided under this Supplemental Plan for Credited Service prior to January 1, 2004, based on Final Average Earnings and Average Incentive Target up to December 31, 2003 and taking into account the early retirement reduction that would have applied if employment had terminated or retirement had occurred on December 31, 2003 but taking into account the maximum pension applicable under the Registered Plan at pension commencement. The letter of credit shall not apply either in respect of Participants subject to US tax as a result of being a US citizen, a US resident or being employed by Bowater Inc. or any affiliated company in the US, unless they have elected in writing to be covered by the letter of credit."
>
> (Emphasis added)

38 [38] However, Petitioners have not been able to locate a resolution of BCFPI Board of Directors amending sections 1.02 and 4.03 of the 2003 SERPs as they read in this 2003 Draft Restatement, nor one resolution adopting the 2003 Draft Restatement.

39 [39] Later on, in July 2009, an officer of BCFPI executed a further restatement of the SERPs, this time "effective January 1, 2003, including amendments up to January 1, 2009 inclusive" (the "**2009 Restatement**")[18]. In that document, the wording of section 4.03 was similar to that of the 2003 Draft Restatement. Yet, the BCFPI Board of Directors did not adopt either a resolution to give effect to this 2009 Restatement.

THE ACTUARIAL VALUATIONS

40 [40] That said, at various times during the relevant years, BCFPI obtained from Mercer actuarial valuations of its liabilities pursuant to the SERPs for the purpose of establishing the face amount of the letter of credit held by RTC.

41 [41] Actuarial valuations as of June 2005 and March 2008 were so performed, in compliance with the 2003 Draft Restatement and the letters sent in 2003 and 2005 to the SERPs members[19].

42 [42] Both the June 2005 and the March 2008 actuarial valuations of Mercer disclosed the following information:

> "To Bowater Canadian Forest Products Inc.
>
> At your request, we have conducted an actuarial valuation of the liabilities as at (...) in respect of certain Supplemental Retirement Plans of Bowater Canadian Forest Products Inc. The purpose of this valuation is to determine the face

> amount of the letter of credit as of such date. We are pleased to present the results of the valuation.
>
> (...)
>
> Based on the terms of the Supplemental Retirement Plans and on notices provided to active and vested terminated members, the letter of credit covers pensions in payment relative to benefits for service up to December 31, 2003 (December 31, 2002 for any member who elected to participate in the DC plan effective January 1, 2003), based on earnings up to December 31, 2003 taking into account the early retirement reductions that would have applied if termination or retirement had occurred on December 31, 2003 and also taking into account the maximum pension applicable at pension commencement.
>
> In accordance with the RCA Trust Agreement between Avenor Inc. and Montreal Trust Company, the amount of the letter of credit shall be equivalent to Bowater Canadian Forest Products lnc.'s determination of its liabilities to beneficiaries. Such determination shall be based on actuarial valuations which the Trustee shall be under no obligation to review or assess."
>
> (Emphasis added)

43 [43] In both valuations, Mercer also indicated that "liabilities correspond only to liabilities for pensions in payment, consistent with the notices provided (by BCFPI) to affected members".

ANALYSIS

44 [44] In the end, this Judgment deals with yet another unfortunate consequence of the insolvency of the Petitioners and their filing for Court protection under the *CCAA*. Simply put, BCFPI does not have the financial resources to continue funding the payment of the SERPs benefits to eligible members. Only the letter of credit remains for those entitled to its proceeds.

45 [45] And still, even if the entitlement is limited to those members identified by the Petitioners in the Motion, according to Schedule F and Mercer's projections[20], there will not be enough to cover everyone for everything they are entitled to under the SERPs. The available funds are expected to run out sometime in January 2026.

46 [46] Be that as it may, the Court must decide the pending issues based upon the interpretation of the relevant sections of the SERPs and the behaviour of the parties in relation thereto.

47 [47] With due respect to the arguments raised by the members listed in Schedules D and E, the Court considers that the Petitioners' position is correct under the circumstances. Only the members listed on Schedules A, B and C are entitled to share in the proceeds of the letter of credit.

48 [48] For what it is worth, this does not negate to the members listed in Schedules D and E their entitlement to the SERPs benefits and their claims in that regard in the context of the restructuring. This Judgment is only concerned with the proceeds of the letter of credit securing, in part, the benefits payable under the SERPs.

49 [49] With respect to the amendments sought by the Petitioners to the Trust Agreement, however, the Court is of the view that it does not have the authority to impose such upon the interested parties in the absence of any consensus on the nature, extent and wording of the provisions at issue.

50 [50] The Court's explanations follow.

1) THE MEMBERS ENTITLED TO SHARE IN THE LETTER OF CREDIT

A) The Canadian Members Who Retired Before December 31, 2003

51 [51] 48 members of the SERPs are Canadian who retired before December 31, 2003. They include the 44 retirees and four beneficiaries listed in Schedule A to the Motion.

52 [52] No one disputes that the benefits of these members are covered by the letter of credit. The Court agrees.

53 [53] The language of the 2003 SERPs provides that the payment of their benefits is to be secured by the letter of credit. They were never advised that their benefits, in whole or in part, were not covered by the letter of credit. The amendments to the 2003 SERPs reflected in the 2003 Draft Restatement and the 2009 Restatement provide that their benefits are covered by the letter of credit. The actuarial valuations prepared by Mercer in 2005 and 2008 included their benefits in the calculation of the amount of the letter of credit.

B) The Canadian Members Who Retired After December 31, 2003

54 [54] Six members of the SERPs are Canadian who retired after December 31, 2003 and before May 26, 2009. They are listed in Schedule B to the Motion.

55 [55] Similarly to the Canadian members who retired before December 31, 2003, no one disputes that the benefits of these members are covered by the letter of credit, as long as they are limited to the benefits accrued up to December 31, 2003. Again, the Court agrees with that assertion.

56 [56] Although the language of the 2003 SERPs provides that the payment of benefits is to be secured by a letter of credit, BCFPI's intention was clearly that only SERPs benefits accrued up to

December 31, 2003, would be secured by the letter of credit.

57 [57] Letters were sent on November 24, 2003 to the SERPs members who were active as of that date in order to advise them that only the benefits of retired SERPs members and only SERPs benefits accrued up to December 31, 2003, would be secured by the letter of credit. This change was also reflected in the 2003 Draft Restatement and the 2009 Restatement.

58 [58] In addition, the actuarial valuations prepared by Mercer in 2005 and 2008 limited the liabilities of the SERPs towards the members who retired after December 31, 2003 to the value of the benefits that accrued up to December 31, 2003, such that the face value of the letter of credit was based on the pre-December 31, 2003 earnings and service.

59 [59] The Court also agrees with Petitioners that Mr. Donald Campbell should be included in that group. He was on salary continuance on April 17, 2009 when the Initial Order was issued. As a result of the Initial Order, his salary continuance was discontinued and his active employment was terminated as of April 15, 2009. Thereafter, Mr. Campbell elected to retire on May 1, 2009.

60 [60] It is appropriate to treat him as a Canadian resident member who retired after December 31, 2003 but before May 26, 2009, as opposed to an active employee.

C) The U.S. Members

61 [61] There were, at the date of the Motion, three members of the SERPs who were U.S. citizens: one retiree who is a Canadian resident (Mr. Warren Woodworth), one beneficiary who is a U.S. resident (Mrs. Alyce Flenniken), and Mr. Jerry Soderberg. All three members of this group retired prior to December 31, 2003. They are listed in Schedule C to the Motion.

62 [62] The SERPs liabilities to Mrs. Flenniken and Mr. Woodworth are covered by the letter of credit. The language of the 2003 SERPs provides that the benefits of all members, including the U.S. members, are covered by the letter of credit and these members have not received any notice or letter from BCFPI whereby they were advised that their benefits, in whole or in part, were not covered by the letter of credit.

63 [63] True, there were, however, negative tax consequences in the United States if the benefits of a U.S. member were secured by a letter of credit. The tax rules of the Internal Revenue Code (the "**IRC**") provided that securing SERPs benefits of SERPs members who were taxpayers of the United States resulted in the obligation for such SERPs members to include in the income for the year during which such security was granted the value of the benefits so secured.

64 [64] For that reason, in the 2003 Draft Restatement and in the 2009 Restatement, it was indicated that the liabilities of the SERPs to the members of this group were not secured by the letter of credit unless they elected in writing to be covered by the letter of credit.

65 [65] Accordingly, the value of the SERPs liabilities to Mrs. Flenniken and Mr. Woodworth were not included in the calculation of the face value of the letter of credit held by RTC in 2005 or 2008. The 2008 actuarial valuation indeed stated:

> "For tax reasons U.S. taxpayers are not covered by the letter of credit unless they elect to be covered. We understand that U.S. taxpayers have been notified by Bowater Canadian Forest Products Inc. to this effect."

66 [66] Nevertheless, the Petitioners do not have any indication in their files that these U.S. members were at any time invited to make such an election. Therefore, their liabilities should have been included in the valuations.

67 [67] As for Mr. Soderberg, also a citizen and resident of the United States, on August 4, 1995, he was given confirmation, through two letters, of changes to his compensation package which included participation in the 1993 SERP[21]. On January 6, 1997, he was advised that his SERPs benefits were secured by a letter of credit held by MTC[22]. On February 25, 1997, he was further advised that although he was and would continue to be a participant of the Avenor America Inc. pension plan (a U.S. pension plan), he would remain entitled to the pension benefits set forth in the letter of August 4, 1995 describing his pension entitlements[23].

68 [68] Still on January 6, 1997, he was granted a Change of Control Agreement by Avenor. During August 1998, there was a change of control, such that the agreement was therefore triggered. On September 3, 1998, Mr. Soderberg was informed of the computation of his benefits pursuant to this Change of Control Agreement and, as a result, fully released and discharged Avenor Inc. and BPPC from all further obligations. He retired on October 1, 1998 and on October 2, 1998[24], he was advised that he would start to receive a pension from the U.S. pension plan and that his SERPs benefits would be assumed by Bowater Inc. and paid from the U.S.

69 [69] Yet, the value of the SERPs liabilities to Mr. Soderberg was not included in the calculation of the face value of the letter of credit held by RTC in 2005 or 2008 because he did not and does not participate in a Canadian registered pension plan.

70 [70] Despite this, based on the above-mentioned letters sent to Mr. Soderberg, the Court agrees with Petitioners that he should also be entitled to continue to receive, from May 1, 2009, his monthly SERPs payments from the proceeds of the letter of credit.

D) The Active Employees and The Deferred Vested Members

71 [71] On May 26, 2009, eleven members of the SERPs were still active employees and six were deferred vested members. They are listed in Schedules D and E to the Motion.

72 [72] Petitioners submit that the benefits of the active employees and the deferred vested members should not be covered by the letter of credit for four main reasons:

- On a proper interpretation, the relevant sections of the SERPs do not allow for it;
- The active employees and the deferred vested members received letters dated November 24, 2003, May 27, 2005, and May 30, 2005 which specified that the letter of credit did not secure the payment of benefits that may become payable some time in the future to active employees or deferred employees;
- The 2003 Draft Restatement and the 2009 Restatement both provided that the letter of credit did not secure benefits during active employment with the corporation or to deferred vested members and shall only apply from pension commencement;
- The actuarial valuations prepared by Mercer in 2005 and 2008 did not include the benefits of the active members and of the deferred vested members.

73 [73] The Court agrees that the active employees listed on Schedule D and the deferred vested members listed on Schedule E are not entitled to receive monthly SERPs payments from the proceeds of the letter of credit.

74 [74] First, it is a reasonable interpretation of the relevant provisions of the SERPs to suggest that the letter of credit covers benefits in payment to the retirees and their beneficiaries, and not the potential future payments to active employees and deferred vested employees.

75 [75] The SERPs are contracts of successive performance. Subsection 4.02 provides that BCFPI shall pay the benefits payable thereunder as they become due.

76 [76] Benefits payable under the SERPs are benefits payable on a monthly basis pursuant to Sections 5 to 11, i.e. on Normal Retirement Date (age 65), Early Retirement Date (age 55), postponed retirement date (after age 65), disability date, death or the date of termination of employment. no benefits are due nor become due before the earliest of such dates.

77 [77] BCFPI's undertaking pursuant to Subsection 4.03 can be interpreted as securing the payment of the benefits provided by the SERPs, not the benefits payable in se or per se. Accordingly, only benefits that are in payment are secured by the letter of credit.

78 [78] The SERPs provide in Subsection 13.08 that their provisions shall be interpreted in accordance with the laws of the Province of Quebec. The relationship between a SERP Participant and BCFPI is contractual and the relevant rules on interpretation are set out in Articles 1425 to 1434 *CCQ*.

79 [79] Pursuant to these rules of interpretation, Subsections 4.02 and 4.03 of the SERPs should not be construed in a vacuum but in relation to each other and other provisions of the SERPs (Article 1427 *CCQ*).

80 [80] Second, under the SERPs, it was for BCFPI to decide on all matters relating to the (i) interpretation, (ii) administration, and (iii) application of the plans.

81 [81] In the exercise of these powers, BCFPI issued the letters dated November 24, 2003 (Exhibit R-8), May 27, 2005 (Exhibit R-9) and May 30, 2005 (Exhibit R-10).

82 [82] The Court agrees that BCFPI's decision to only secure benefits in payment and not benefits under accrual was a reasonable decision reached pursuant to Subsection 14.01.

83 [83] When such decisions are reasonable and reached without consideration of reasons or motives that are outside of the scope of the discretion granted to the "decision-making person", the Courts will not lightly intervene in the "decision-making" process[25].

84 [84] As can be seen from the language of the 2003 and 2005 letters, there were reasonable reasons for BCFPI to reach such decisions. In *James Robert Marchant* v. *The Royal Trust Company* and *Bowater Pulp and Paper Canada Inc.*[26], the Court upheld the administrator's decision to deny an enhanced benefit since the decision was reasonable and not taken in bad faith.

85 [85] Third, even if the letters and notices sent in 2003 and 2005 were viewed as amendments to the SERPs rather than interpretation, administration or application of the SERPs, they were nevertheless valid amendments pursuant to Subsection 15.01.

86 [86] This provision imposes three conditions to the validity of an amendment:

1) The amendment must be communicated in writing by BCFPI to the Participants;
2) The communication must indicate the effective date of the amendment which must not precede the date that the communication is deemed to have been received by the Participants; and
3) The amendment must be made in respect of all Participants, excluding those who have already commenced to receive benefits under the SERPs.

87 [87] These conditions were met here. The letters were communicated in writing by BCFPI to the Participants in accordance with the first condition. The first letter was dated November 24, 2003 and came into effect on January 1, 2004. The second letters were dated May 27 and 30, 2005 and came into effect immediately. Therefore, the three letters met the second condition. Finally, the amendment affected all active employees and deferred vested members, as required by the third condition.

88 [88] That is not all.

89 [89] The validity of the letters was never challenged by any active employee or deferred vested employee before the current proceedings. This is quite telling. In matters of contractual

interpretation, Article 1426 *CCQ* states that the interpretation given by the parties and their behaviour in that regard are factors to be taken into account.

90 [90] In comparison, the subsequent behaviour of both BCFPI and Mercer was in strict compliance with such changes.

91 [91] The mentions appearing in the 2003 Draft Restatement and 2009 Restatement cited before show clearly that it was either BCFPI's interpretation, administration or application of the SERPs that the letter of credit guaranteed only the benefits then in payment to the retirees or their beneficiaries or, at the very least, its definite intention to amend the SERPs along those lines.

92 [92] It is true that BCFPI has not been able to locate a resolution of its Board of Directors amending Subsections 1.02 and 4.03 of the SERPs as they read in the 2003 Draft Restatement, nor adopting the 2003 Draft Restatement. It is also true that the Board of Directors did not adopt a resolution to give effect to the 2009 Restatement.

93 [93] Nevertheless, this is not fatal to the validity of BCFPI's decision respecting the interpretation, administration and application of the plans or the amendments brought about by the 2003 and 2005 letters.

94 [94] The active employees and the deferred vested employees who have contested the Motion allege that a resolution of the Board of Directors was required to modify the SERPs or to authorize officers to modify the SERPs.

95 [95] However, they have not pointed to any provision of BCFPI's articles or by-laws that would require such a resolution for such an amendment. Moreover, nothing in the *Canada Business Corporations Act* ("***CBCA***") requires a board resolution in such a case.

96 [96] At worst, the active employees and deferred vested employees can argue that the delegation to Mr. Cabana, the V.P. Human Resources & Public Affairs, Canadian Operations of BCFPI who signed the letters at issue, was not in accordance with Subsection 14.02 of the SERPs.

97 [97] If that is the argument, there has been subsequent ratification by BCFPI, whether through the employer certifications referred to in the Mercer valuations and executed by another officer, or through the provision of a letter of credit that was calculated without taking into account the benefits that would have eventually become due to the active employees and the deferred vested employees.

98 [98] In addition, Section 16(3) of the *CBCA* provides a safe harbour as follows:

> "(3) Rights preserved - no act of a corporation, including any transfer of property to or by a corporation, is invalid by reason only that the act or transfer is contrary to its articles or this Act."

99 [99] Lastly, on that point, Maurice and Paul Martel are of the opinion that the co-contracting party ("*le tiers*") cannot attack the contract by invoking internal corporate irregularities such as the lack of appropriate authorization[27]:

> "*Donc, lorsqu'une irrégularité de régie interne entache une transaction, elle ne peut être invoquée par le tiers pour faire annuler cette transaction. Seule la compagnie ou un de ses actionnaires pourrait l'invoquer. Quant à la compagnie, une telle démarche est vouée à l'échec dès le départ si elle veut l'entreprendre pour faire annuler la transaction, car le tiers est protégé par la règle de l'indoor management. Reste l'actionnaire: il ne pourrait pas faire annuler la transaction, car la règle de l'indoor management joue ici encore en faveur du tiers. D'ailleurs, il n'est même pas sûr que l'actionnaire jouisse d'un tel recours, surtout si l'irrégularité a été ratifiée par la majorité des actionnaires.*"

100 [100] In closing, from a mere practical standpoint, one could add that pursuant to the Mercer actuarial valuations, the amount of the letter of credit was based on the assumption that only retirees and their beneficiaries were covered by the letter of credit, with the result that funds have not been put aside for the active employees and the deferred vested employees. Any deficit that already exists in terms of the coverage of the benefits payable to retirees would therefore be increased if they were included.

101 [101] Moreover, neither the calculation of the SERPs benefits of the active employees and the deferred vested employees, nor the way in which the active employees and the deferred vested employees would benefit from the letter of credit, is clear. In fact, both would create problems because of the number of unknown assumptions that would likely influence the calculations of any benefits.

102 [102] The Court will therefore limit the SERPs members' entitlement to the proceeds of the letter of credit to the members listed in Schedules A, B and C to the Motion. As requested by the Petitioners, this conclusion will be binding upon all SERPs members. The Court is satisfied that the Motion, be it in its original or amended forms, has been duly communicated to the Service List and to the attorneys who have appeared on behalf of many of the members, while being at the same time always sent by registered mail to all SERPs members and posted on the Monitor's website.

103 [103] That said, there are, in principle, three ways in which the proceeds of the letter of credit can be distributed to the members entitled to share in those:

a) RTC can continue to make monthly payments to the members entitled to share in the proceeds of the letter of credit until the funds are exhausted. By Judgment rendered July 2, 2010, the Court, with the consent of everyone, has already ordered RTC to resume the monthly payments to the members listed in Schedules A, B and C to the Motion for all outstanding arrears payable since May 1, 2009;

b) RTC can distribute the balance of the proceeds on a pro rata basis based on the value of each member's benefits as at the date of this Judgment; or
c) RTC can distribute the balance of the proceeds on a pro rata basis based on the value of each member's benefits as at May 26, 2009.

104 [104] The Court agrees with Petitioners that the first approach is to be preferred for the time being. It is fairer to the members entitled to receive monthly SERPs payments from the proceeds of the letter of credit. It is, in fact, in accordance with the approach already followed by the Court in its Judgment of July 2, 2010.

105 [105] Conversely, the second and third approaches would likely require an amendment to the SERPs and the Trust Agreement in order to pay lump sums, which creates a problem under the circumstances, as will be discussed below.

106 [106] Since there is no real debate on the entitlement of the members listed in Schedules A, B and C to receive their monthly SERPs payments from the proceeds of the letter of credit, and in view of the advanced age of many of these members, it is appropriate to order the provisional execution of this Judgment notwithstanding appeal.

2. AMENDMENTS TO THE TRUST AGREEMENT

107 [107] In the Motion, BCFPI asks the Court to also authorize it to amend the Trust Agreement entered into with RTC, notably to dissociate itself from all of its obligations under the Trust Agreement.

108 [108] There is no provision in the Trust Agreement dealing with amendments and the interested parties, including BCFPI, RTC or, for that matter, the members listed in Schedules A, B and C to the Motion, do not agree on the nature, extent or wording of the amendments sought.

109 [109] Under these circumstances, the Court considers that the Trust Agreement entered into between BCFPI and RTC cannot be amended and that BCFPI cannot ask the Court to modify it. This negotiation belongs to the parties themselves. It is not for the Court to substitute itself to this process.

110 [110] It is inappropriate for a Court to attempt to draw up a contract for the parties when these parties do not agree to modify its contractual terms. Contracts represent a law which private parties have agreed applies to them and they normally cannot be varied by the Courts. This remains true as well in the context of a *CCAA* restructuring[28].

111 [111] Without RTC's consent, BCFPI cannot have the Trust Agreement amended to remove all of its rights and obligations and give those rights and obligations to a committee of beneficiaries.

112 [112] For the time being, the Trust Agreement entered into between BCFPI and RTC is still

in force and has not been terminated.

113 [113] Although BCFPI contemplates terminating the SERPs to replace them with new SERPs that are described in section 6.9 of the Plan of Arrangement[29], and argues that the termination of the SERPs entails the termination of the Trust Agreement, this Plan of Arrangement is yet to be voted upon and sanctioned by the Court.

114 [114] Indeed, based on the representations made at hearing, it appears that the interested parties do not even agree on the impact of the potential termination of the SERPs upon the Trust Agreement.

115 [115] This issue, if it ever arises, will have to be dealt with in due course. For the purposes of this Judgment, it is not necessary to decide this question and rule upon the potential consequences that may follow from any answer.

116 [116] For now, it will suffice to state that RTC will continue the monthly payments of SERPs benefits from the proceeds of the letter of credit in conformity with the terms of this Judgment up until the earlier of the date on which the Trust Agreement is terminated or a further order of the Court.

117 [117] That said, in its contestation to the amendments sought by the Petitioners to the Trust Agreement, RTC itself seeks declarations that the RCA Plan Trust Fund were properly invested in 30-day Government of Canada Treasury Bills and that it shall not be liable for any damage or complaint relating to these investments.

118 [118] These declarations are not necessary. The provisions of the Trust Agreement govern the rights and obligations of the interested parties. Short of any difficulties or disagreements that no one alluded to, it is not for the Court to give advanced rulings on potential future disputes.

119 [119] RTC also seeks declarations that it shall not be liable for any delays caused by the filing of the Motion, in a context where no one appears to raise any issue in that regard. This declaration is again unnecessary.

120 [120] Finally, RTC wants a declaration that it cannot be held liable for any consequence of its reliance upon the decision to be rendered by the Court on the Motion. The Court's conclusions are, of course, binding upon those that are subject to their terms. They are quite sufficient as they stand for any concerned parties to conduct themselves accordingly. It is not the role of the Court to go any further than that.

FOR THESE REASONS, THE COURT:

121 [1] **GRANTS, BUT IN PART ONLY** the Re-Amended Motion for Directions on the Identity of the Persons Whose Benefits Under the Bowater Supplemental Executive Retirement

Plans Were Secured by a Letter of Credit (the "**Motion**");

122 [2] **EXEMPTS**, if applicable, the Petitioners from any further service of the Motion and from any further notice or delay of presentation;

123 [3] **DECLARES** that the service of the Motion by registered mail or mail to the SERPs members, who are not represented by attorneys, is valid;

124 [4] **DECLARES** that this Judgment is binding on all members of the SERPs and their beneficiaries;

125 [5] **DECLARES** that only the following members of the SERPs benefit from the letter of credit (Exhibit R-7) and are entitled to receive, from May 1, 2009, monthly SERPs payments from the proceeds of the letter of credit (Exhibit R-7) held by The Royal Trust Company ("RTC"):

a) The Canadian resident members of the SERPs who retired before December 31, 2003 (listed in Schedule A to the Motion);
b) The Canadian resident members of the SERPs who retired after December 31, 2003 but before May 26, 2009, including Mr. Donald Campbell (listed in Schedule B to the Motion), but only on the value of their SERPs benefits accrued up to December 31, 2003; and
c) The U.S. members of the SERPs, including Mr. Jerry Soderberg (listed in Schedule C to the Motion);

126 [6] **DECLARES** that the Active Employees and the Deferred Vested Employees whose names are listed in Schedules D and E to the Motion are not entitled to have the value of their accrued benefits under the SERPs secured by the amount held by RTC and that no person other than the persons referred to in the preceding paragraph is entitled to have the value of his or her accrued benefits under the SERPs secured by the amount held by the RTC, nor to receive any monthly SERPs payment from the proceeds of the letter of credit (Exhibit R-7) held by RTC;

127 [7] **ORDERS** RTC, up until the earlier of the date on which the Trust Agreement (Exhibit R-5) is terminated or a further order of the Court, to continue the monthly SERPs payments, without interest, from the proceeds of the letter of credit (Exhibit R-7), in conformity with the terms of this Judgment;

128 [8] **DECLARES** that, for the purpose of the Trust Agreement (Exhibit R-5), RTC acting in accordance with this Judgment shall be construed and have the same effect as if RTC relied and acted upon the written instructions of Bowater Canadian Forest Products Inc;

129 [9] **ORDERS** the provisional execution of this Judgment notwithstanding any appeal and without the necessity of furnishing any security;

130 [10] **WITHOUT COSTS.**

CLÉMENT GASCON, J.S.C.

* * * * *

SCHEDULE "A"

ABITIBI PETITIONERS

1. **ABITIBI-CONSOLIDATED INC.**
2. **ABITIBI-CONSOLIDATED COMPANY OF CANADA**
3. **3224112 NOVA SCOTIA LIMITED**
4. **MARKETING DONOHUE INC.**
5. **ABITIBI-CONSOLIDATED CANADIAN OFFICE PRODUCTS HOLDINGS INC.**
6. **3834328 CANADA INC.**
7. **6169678 CANADA INC.**
8. **4042140 CANADA INC.**
9. **DONOHUE RECYCLING INC.**
10. **1508756 ONTARIO INC.**
11. **3217925 NOVA SCOTIA COMPANY**
12. **LA TUQUE FOREST PRODUCTS INC.**
13. **ABITIBI-CONSOLIDATED NOVA SCOTIA INCORPORATED**
14. **SAGUENAY FOREST PRODUCTS INC.**
15. **TERRA NOVA EXPLORATIONS LTD.**
16. **THE JONQUIERE PULP COMPANY**
17. **THE INTERNATIONAL BRIDGE AND TERMINAL COMPANY**
18. **SCRAMBLE MINING LTD.**
19. **9150-3383 QUÉBEC INC.**
20. **ABITIBI-CONSOLIDATED (U.K.) INC.**

SCHEDULE "B"

BOWATER PETITIONERS

1. **BOWATER CANADIAN HOLDINGS INC.**
2. **BOWATER CANADA FINANCE CORPORATION**
3. **BOWATER CANADIAN LIMITED**
4. **3231378 NOVA SCOTIA COMPANY**
5. **ABITIBIBOWATER CANADA INC.**
6. **BOWATER CANADA TREASURY CORPORATION**
7. **BOWATER CANADIAN FOREST PRODUCTS INC.**

8. **BOWATER SHELBURNE CORPORATION**
9. **BOWATER LAHAVE CORPORATION**
10. **ST-MAURICE RIVER DRIVE COMPANY LIMITED**
11. **BOWATER TREATED WOOD INC.**
12. **CANEXEL HARDBOARD INC.**
13. **9068-9050 QUÉBEC INC.**
14. **ALLIANCE FOREST PRODUCTS (2001) INC.**
15. **BOWATER BELLEDUNE SAWMILL INC.**
16. **BOWATER MARITIMES INC.**
17. **BOWATER MITIS INC.**
18. **BOWATER GUÉRETTE INC.**
19. **BOWATER COUTURIER INC.**

SCHEDULE "C"

18.6 CCAA PETITIONERS

1. **ABITIBIBOWATER INC.**
2. **ABITIBIBOWATER US HOLDING 1 CORP.**
3. **BOWATER VENTURES INC.**
4. **BOWATER INCORPORATED**
5. **BOWATER NUWAY INC.**
6. **BOWATER NUWAY MID-STATES INC.**
7. **CATAWBA PROPERTY HOLDINGS LLC**
8. **BOWATER FINANCE COMPANY INC.**
9. **BOWATER SOUTH AMERICAN HOLDINGS INCORPORATED**
10. **BOWATER AMERICA INC.**
11. **LAKE SUPERIOR FOREST PRODUCTS INC.**
12. **BOWATER NEWSPRINT SOUTH LLC**
13. **BOWATER NEWSPRINT SOUTH OPERATIONS LLC**
14. **BOWATER FINANCE II, LLC**
15. **BOWATER ALABAMA LLC**
16. **COOSA PINES GOLF CLUB HOLDINGS LLC**

1 Exhibit R-17.

2 Exhibit R-18.

3 Exhibit R-7.

4 Re-Amended Motion for Directions on the Identity of the Persons Whose Benefits Under the Bowater Supplemental Executive Retirement Plans Were Secured by a Letter of Credit dated July 2, 2010 (the "**Motion**").

5 Exhibit R-29.

6 Exhibit R-1.

7 Exhibit R-2.

8 Exhibit R-3.

9 Exhibit R-4.

10 Exhibit R-5.

11 Exhibit R-5.

12 Exhibit R-6.

13 Exhibit R-7.

14 Exhibit R-8.

15 Exhibit R-9.

16 Exhibit R-10.

17 Exhibit R-11.

18 Exhibit R-13.

19 Exhibits R-15 and R-16.

20 Exhibit R-31.

21 Exhibit R-24.

22 Exhibit R-25.

23 Exhibit R-26.

24 Exhibit R-28.

25 See *Neville* v. *Wynne*, 2005 BCSC 483, confirmed 2006 BCCA 460, and *Patrick Communications Inc.* v. *Telus*, 2006 BCSC 854, confirmed 2007 BCCA 200.

26 (1999), 26 C.C.P.B. 126, (S.C., 1999-09-30), SOQUIJ AZ-99026555.

27 Maurice MARTEL et Paul MARTEL, *La Compagnie au Québec: les aspects juridiques* v. 1, Montreal: Wilson & Lafleur/Martel ltée, 2010, paragraph 26-20.

28 *Allarco Entertainment Inc. (Re)*, [2009] A.J. No. 996, 2009 CarswellAlta 1458 (Alta. Q.B.).

29 Exhibit R-32.

TAB 2

4 of 4 DOCUMENTS

Indexed as:

Century Services Inc. v. Canada (Attorney General)

Century Services Inc. Appellant;
v.
Attorney General of Canada on behalf of Her Majesty The Queen in Right of Canada Respondent.

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[2010] 3 R.C.S. 379

[2010] S.C.J. No. 60

[2010] A.C.S. no 60

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72 C.B.R. (5th) 170

12 B.C.L.R. (5th) 1

296 B.C.A.C. 1

326 D.L.R. (4th) 577

409 N.R. 201

[2011] 2 W.W.R. 383

File No.: 33239.

Supreme Court of Canada

Heard: May 11, 2010;
Judgment: December 16, 2010.

Present: McLachlin C.J. and Binnie, LeBel, Deschamps, Fish, Abella, Charron, Rothstein and Cromwell JJ.

(136 paras.)

Appeal From:

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

Catchwords:

Bankruptcy and Insolvency -- Priorities -- Crown applying on eve of bankruptcy of debtor company to have GST monies held in trust paid to Receiver General of Canada -- Whether deemed trust in favour of Crown under Excise Tax Act prevails over provisions of Companies' Creditors Arrangement Act purporting to nullify deemed trusts in favour of Crown -- Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 18.3(1) -- Excise Tax Act, R.S.C. 1985, c. E-15, s. 222(3).

Bankruptcy and insolvency -- Procedure -- Whether chambers judge had authority to make order partially lifting stay of proceedings to allow debtor company to make assignment in bankruptcy and to stay Crown's right to enforce GST deemed trust -- Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.

Trusts -- Express trusts -- GST collected but unremitted to Crown -- Judge ordering that GST be held by Monitor in trust account -- Whether segregation of Crown's GST claim in Monitor's account created an express trust in favour of Crown.

[page380]

Summary:

The debtor company commenced proceedings under the *Companies' Creditors Arrangement Act* ("*CCAA*"), obtaining a stay of proceedings to allow it time to reorganize its financial affairs. One of the debtor company's outstanding debts at the commencement of the reorganization was an amount of unremitted Goods and Services Tax ("GST") payable to the Crown. Section 222(3) of the *Excise Tax Act* ("*ETA*") created a deemed trust over unremitted GST, which operated despite any other enactment of Canada except the *Bankruptcy and Insolvency Act* ("*BIA*"). However, s. 18.3(1) of the *CCAA* provided that any statutory deemed trusts in favour of the Crown did not operate under the *CCAA*, subject to certain exceptions, none of which mentioned GST.

Pursuant to an order of the *CCAA* chambers judge, a payment not exceeding $5 million was approved to the debtor company's major secured creditor, Century Services. However, the chambers

judge also ordered the debtor company to hold back and segregate in the Monitor's trust account an amount equal to the unremitted GST pending the outcome of the reorganization. On concluding that reorganization was not possible, the debtor company sought leave of the court to partially lift the stay of proceedings so it could make an assignment in bankruptcy under the *BIA*. The Crown moved for immediate payment of unremitted GST to the Receiver General. The chambers judge denied the Crown's motion, and allowed the assignment in bankruptcy. The Court of Appeal allowed the appeal on two grounds. First, it reasoned that once reorganization efforts had failed, the chambers judge was bound under the priority scheme provided by the *ETA* to allow payment of unremitted GST to the Crown and had no discretion under s. 11 of the *CCAA* to continue the stay against the Crown's claim. Second, the Court of Appeal concluded that by ordering the GST funds segregated in the Monitor's trust account, the chambers judge had created an express trust in favour of the Crown.

Held (Abella J. dissenting): The appeal should be allowed.

Per McLachlin C.J. and Binnie, LeBel, Deschamps, Charron, Rothstein and Cromwell JJ.: The apparent conflict between s. 222(3) of the *ETA* and s. 18.3(1) of the *CCAA* can be resolved through an interpretation that properly recognizes the history of the *CCAA*, its function amidst the body of insolvency legislation enacted by [page381] Parliament and the principles for interpreting the *CCAA* that have been recognized in the jurisprudence. The history of the *CCAA* distinguishes it from the *BIA* because although these statutes share the same remedial purpose of avoiding the social and economic costs of liquidating a debtor's assets, the *CCAA* offers more flexibility and greater judicial discretion than the rules-based mechanism under the *BIA*, making the former more responsive to complex reorganizations. Because the *CCAA* is silent on what happens if reorganization fails, the *BIA* scheme of liquidation and distribution necessarily provides the backdrop against which creditors assess their priority in the event of bankruptcy. The contemporary thrust of legislative reform has been towards harmonizing aspects of insolvency law common to the *CCAA* and the *BIA*, and one of its important features has been a cutback in Crown priorities. Accordingly, the *CCAA* and the *BIA* both contain provisions nullifying statutory deemed trusts in favour of the Crown, and both contain explicit exceptions exempting source deductions deemed trusts from this general rule. Meanwhile, both Acts are harmonious in treating other Crown claims as unsecured. No such clear and express language exists in those Acts carving out an exception for GST claims.

When faced with the apparent conflict between s. 222(3) of the *ETA* and s. 18.3(1) of the *CCAA*, courts have been inclined to follow *Ottawa Senators Hockey Club Corp. (Re)* and resolve the conflict in favour of the *ETA*. *Ottawa Senators* should not be followed. Rather, the *CCAA* provides the rule. Section 222(3) of the *ETA* evinces no explicit intention of Parliament to repeal *CCAA* s. 18.3. Where Parliament has sought to protect certain Crown claims through statutory deemed trusts and intended that these deemed trusts continue in insolvency, it has legislated so expressly and elaborately. Meanwhile, there is no express statutory basis for concluding that GST claims enjoy a preferred treatment under the *CCAA* or the *BIA*. The internal logic of the *CCAA* appears to subject a GST deemed trust to the waiver by Parliament of its priority. A strange asymmetry would result if

differing treatments of GST deemed trusts under the *CCAA* and the *BIA* were found to exist, as this would encourage statute shopping, undermine the *CCAA*'s remedial purpose and invite the very social ills that the statute was enacted to avert. The later in time enactment of the more general s. 222(3) of the *ETA* does not require application of the doctrine of implied repeal to the earlier and more specific s. 18.3(1) of the *CCAA* in the circumstances of this case. In any event, [page382] recent amendments to the *CCAA* in 2005 resulted in s. 18.3 of the Act being renumbered and reformulated, making it the later in time provision. This confirms that Parliament's intent with respect to GST deemed trusts is to be found in the *CCAA*. The conflict between the *ETA* and the *CCAA* is more apparent than real.

The exercise of judicial discretion has allowed the *CCAA* to adapt and evolve to meet contemporary business and social needs. As reorganizations become increasingly complex, *CCAA* courts have been called upon to innovate. In determining their jurisdiction to sanction measures in a *CCAA* proceeding, courts should first interpret the provisions of the *CCAA* before turning to their inherent or equitable jurisdiction. Noteworthy in this regard is the expansive interpretation the language of the *CCAA* is capable of supporting. The general language of the *CCAA* should not be read as being restricted by the availability of more specific orders. The requirements of appropriateness, good faith and due diligence are baseline considerations that a court should always bear in mind when exercising *CCAA* authority. The question is whether the order will usefully further efforts to avoid the social and economic losses resulting from liquidation of an insolvent company, which extends to both the purpose of the order and the means it employs. Here, the chambers judge's order staying the Crown's GST claim was in furtherance of the *CCAA*'s objectives because it blunted the impulse of creditors to interfere in an orderly liquidation and fostered a harmonious transition from the *CCAA* to the *BIA*, meeting the objective of a single proceeding that is common to both statutes. The transition from the *CCAA* to the *BIA* may require the partial lifting of a stay of proceedings under the *CCAA* to allow commencement of *BIA* proceedings, but no gap exists between the two statutes because they operate in tandem and creditors in both cases look to the *BIA* scheme of distribution to foreshadow how they will fare if the reorganization is unsuccessful. The breadth of the court's discretion under the *CCAA* is sufficient to construct a bridge to liquidation under the *BIA*. Hence, the chambers judge's order was authorized.

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No express trust was created by the chambers judge's order in this case because there is no certainty of object inferrable from his order. Creation of an express trust requires certainty of intention, subject matter and object. At the time the chambers judge accepted the proposal to segregate the monies in the Monitor's trust account there was no certainty that the Crown would be the beneficiary, or object, of the trust because exactly who might take the money in the final result was in doubt. In any event, no dispute over the money would even arise under the interpretation of s. 18.3(1) of the *CCAA* established above, because the Crown's deemed trust priority over GST claims would be lost under the *CCAA* and the Crown would rank as an unsecured creditor for this amount.

Per Fish J.: The GST monies collected by the debtor are not subject to a deemed trust or priority in favour of the Crown. In recent years, Parliament has given detailed consideration to the Canadian insolvency scheme but has declined to amend the provisions at issue in this case, a deliberate exercise of legislative discretion. On the other hand, in upholding deemed trusts created by the *ETA* notwithstanding insolvency proceedings, courts have been unduly protective of Crown interests which Parliament itself has chosen to subordinate to competing prioritized claims. In the context of the Canadian insolvency regime, deemed trusts exist only where there is a statutory provision creating the trust and a *CCAA* or *BIA* provision explicitly confirming its effective operation. The *Income Tax Act*, the *Canada Pension Plan* and the *Employment Insurance Act* all contain deemed trust provisions that are strikingly similar to that in s. 222 of the *ETA* but they are all also confirmed in s. 37 of the *CCAA* and in s. 67(3) of the *BIA* in clear and unmistakeable terms. The same is not true of the deemed trust created under the *ETA*. Although Parliament created a deemed trust in favour of the Crown to hold unremitted GST monies, and although it purports to maintain this trust notwithstanding any contrary federal or provincial legislation, it did not confirm the continued operation of the trust in either the *BIA* or the *CCAA*, reflecting Parliament's intention to allow the deemed trust to lapse with the commencement of insolvency proceedings.

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Per Abella J. (dissenting): Section 222(3) of the *ETA* gives priority during *CCAA* proceedings to the Crown's deemed trust in unremitted GST. This provision unequivocally defines its boundaries in the clearest possible terms and excludes only the *BIA* from its legislative grasp. The language used reflects a clear legislative intention that s. 222(3) would prevail if in conflict with any other law except the *BIA*. This is borne out by the fact that following the enactment of s. 222(3), amendments to the *CCAA* were introduced, and despite requests from various constituencies, s. 18.3(1) was not amended to make the priorities in the *CCAA* consistent with those in the *BIA*. This indicates a deliberate legislative choice to protect the deemed trust in s. 222(3) from the reach of s. 18.3(1) of the *CCAA*.

The application of other principles of interpretation reinforces this conclusion. An earlier, specific provision may be overruled by a subsequent general statute if the legislature indicates, through its language, an intention that the general provision prevails. Section 222(3) achieves this through the use of language stating that it prevails despite any law of Canada, of a province, or "any other law" other than the *BIA*. Section 18.3(1) of the *CCAA* is thereby rendered inoperative for purposes of s. 222(3). By operation of s. 44(*f*) of the *Interpretation Act*, the transformation of s. 18.3(1) into s. 37(1) after the enactment of s. 222(3) of the *ETA* has no effect on the interpretive queue, and s. 222(3) of the *ETA* remains the "later in time" provision. This means that the deemed trust provision in s. 222(3) of the *ETA* takes precedence over s. 18.3(1) during *CCAA* proceedings. While s. 11 gives a court discretion to make orders notwithstanding the *BIA* and the *Winding-up Act*, that discretion is not liberated from the operation of any other federal statute. Any exercise of discretion is therefore circumscribed by whatever limits are imposed by statutes other than the *BIA* and the

Winding-up Act. That includes the *ETA*. The chambers judge in this case was, therefore, required to respect the priority regime set out in s. 222(3) of the *ETA*. Neither s. 18.3(1) nor s. 11 of the *CCAA* gave him the authority to ignore it. He could not, as a result, deny the Crown's request for payment of the GST funds during the *CCAA* proceedings.

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Overruled: *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737; **distinguished:** *Doré v. Verdun (City)*, [1997] 2 S.C.R. 862; **referred to:** *Reference re Companies' Creditors Arrangement Act*, [1934] S.C.R. 659; *Quebec (Revenue) v. Caisse populaire Desjardins de Montmagny*, 2009 SCC 49, [2009] 3 S.C.R. 286; *Deputy Minister of Revenue v. Rainville*, [1980] 1 S.C.R. 35; *Gauntlet Energy Corp., Re*, 2003 ABQB 894, 30 Alta. L.R. (4) 192; *Komunik Corp. (Arrangement relatif à)*, 2009 QCCS 6332 (CanLII), leave to appeal granted, 2010 QCCA 183 (CanLII); *Royal Bank of Canada v. Sparrow Electric Corp.*, [1997] 1 S.C.R. 411; *First Vancouver Finance v. M.N.R.*, 2002 SCC 49, [2002] 2 S.C.R. 720; *Solid Resources Ltd., Re* (2002), 40 C.B.R. (4) 219; *Metcalfe & Mansfield Alternative Investments II Corp. (Re)*, 2008 ONCA 587, 92 O.R. (3d) 513; *Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106; *Elan Corp. v. Comiskey* (1990), 41 O.A.C. 282; *Chef Ready Foods Ltd. v. Hongkong Bank of Can.* (1990), 51 B.C.L.R. (2d) 84; *Pacific National Lease Holding Corp., Re* (1992), 19 B.C.A.C. 134; *Canadian Airlines Corp., Re*, 2000 ABQB 442, 84 Alta. L.R. (3d) 9; *Air Canada, Re* (2003), 42 C.B.R. (4) 173; *Air Canada, Re*, 2003 CanLII 49366; *Canadian Red Cross Society/Société Canadienne de la Croix Rouge, Re* (2000), 19 C.B.R. (4) 158; *Skydome Corp., Re* (1998), 16 C.B.R. (4) 118; *United Used Auto & Truck Parts Ltd., Re*, 2000 BCCA 146, 135 B.C.A.C. 96, aff'g (1999), 12 C.B.R. (4) 144; *Skeena Cellulose Inc., Re*, 2003 BCCA 344, 13 B.C.L.R. (4) 236; *Stelco Inc. (Re)* (2005), 75 O.R. (3d) 5; *Philip's Manufacturing Ltd., Re* (1992), 9 C.B.R. (3d) 25; *Ivaco Inc. (Re)* (2006), 83 O.R. (3d) 108.

By Fish J.

Referred to: *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737.

By Abella J. (dissenting)

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History and Disposition:

APPEAL from a judgment of the British Columbia Court of Appeal (Newbury, Tysoe and Smith JJ.A.), 2009 BCCA 205, 98 B.C.L.R. (4) 242, 270 B.C.A.C. 167, 454 W.A.C. 167, [2009] 12 W.W.R. 684, [2009] G.S.T.C. 79, [2009] B.C.J. No. 918 (QL), 2009 CarswellBC 1195, reversing a judgment of Brenner C.J.S.C., 2008 BCSC 1805, [2008] G.S.T.C. 221, [2008] B.C.J. No. 2611 (QL), 2008 CarswellBC 2895, dismissing a Crown application for payment of GST monies. Appeal allowed, Abella J. dissenting.

Counsel:

Mary I. A. Buttery, *Owen J. James* and *Matthew J. G. Curtis*, for the appellant.

Gordon Bourgard, *David Jacyk* and *Michael J. Lema*, for the respondent.

The judgment of McLachlin C.J. and Binnie, LeBel, Deschamps, Charron, Rothstein and Cromwell JJ. was delivered by

1 DESCHAMPS J.:-- For the first time this Court is called upon to directly interpret the provisions of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). In that respect, two questions are raised. The first requires reconciliation of provisions of the *CCAA* and the *Excise Tax Act*, R.S.C. 1985, c. E-15 ("*ETA*"), which lower courts have held to be in conflict with one another. The second concerns the scope of a court's discretion when supervising reorganization. The relevant statutory provisions are reproduced in the Appendix. On the first question, having considered the evolution of Crown priorities in the context of insolvency and the wording of the various statutes creating Crown priorities, I conclude that it is the *CCAA* and not the *ETA* that provides the rule. On the second question, I conclude that the broad discretionary jurisdiction conferred on the supervising judge must be interpreted having regard to the remedial nature of the *CCAA* and insolvency legislation generally. Consequently, the court had the discretion to partially lift a stay of proceedings to allow the debtor to make an assignment under the *Bankruptcy and Insolvency [page389] Act*, R.S.C. 1985, c. B-3 ("*BIA*"). I would allow the appeal.

1. Facts and Decisions of the Courts Below

2 Ted LeRoy Trucking Ltd. ("LeRoy Trucking") commenced proceedings under the *CCAA* in the Supreme Court of British Columbia on December 13, 2007, obtaining a stay of proceedings with a view to reorganizing its financial affairs. LeRoy Trucking sold certain redundant assets as authorized by the order.

3 Amongst the debts owed by LeRoy Trucking was an amount for Goods and Services Tax ("GST") collected but unremitted to the Crown. The *ETA* creates a deemed trust in favour of the Crown for amounts collected in respect of GST. The deemed trust extends to any property or proceeds held by the person collecting GST and any property of that person held by a secured creditor, requiring that property to be paid to the Crown in priority to all security interests. The *ETA* provides that the deemed trust operates despite any other enactment of Canada except the *BIA*. However, the *CCAA* also provides that subject to certain exceptions, none of which mentions GST, deemed trusts in favour of the Crown do not operate under the *CCAA*. Accordingly, under the *CCAA* the Crown ranks as an unsecured creditor in respect of GST. Nonetheless, at the time LeRoy Trucking commenced *CCAA* proceedings the leading line of jurisprudence held that the *ETA* took precedence over the *CCAA* such that the Crown enjoyed priority for GST claims under the *CCAA*, even though it would have lost that same priority under the *BIA*. The *CCAA* underwent substantial amendments in 2005 in which some of the provisions at issue in this appeal were renumbered and reformulated (S.C. 2005, c. 47). However, these amendments only came into force on September 18, 2009. I will refer to the amended provisions only where relevant.

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4 On April 29, 2008, Brenner C.J.S.C., in the context of the *CCAA* proceedings, approved a payment not exceeding $5 million, the proceeds of redundant asset sales, to Century Services, the debtor's major secured creditor. LeRoy Trucking proposed to hold back an amount equal to the GST monies collected but unremitted to the Crown and place it in the Monitor's trust account until the outcome of the reorganization was known. In order to maintain the *status quo* while the success of the reorganization was uncertain, Brenner C.J.S.C. agreed to the proposal and ordered that an amount of $305,202.30 be held by the Monitor in its trust account.

5 On September 3, 2008, having concluded that reorganization was not possible, LeRoy Trucking sought leave to make an assignment in bankruptcy under the *BIA*. The Crown sought an order that the GST monies held by the Monitor be paid to the Receiver General of Canada. Brenner C.J.S.C. dismissed the latter application. Reasoning that the purpose of segregating the funds with the Monitor was "to facilitate an ultimate payment of the GST monies which were owed pre-filing, but only if a viable plan emerged", the failure of such a reorganization, followed by an assignment in bankruptcy, meant the Crown would lose priority under the *BIA* (2008 BCSC 1805, [2008] G.S.T.C.

221).

6 The Crown's appeal was allowed by the British Columbia Court of Appeal (2009 BCCA 205, 270 B.C.A.C. 167). Tysoe J.A. for a unanimous court found two independent bases for allowing the Crown's appeal.

7 First, the court's authority under s. 11 of the *CCAA* was held not to extend to staying the Crown's application for immediate payment of the GST funds subject to the deemed trust after it was clear that reorganization efforts had failed and [page391] that bankruptcy was inevitable. As restructuring was no longer a possibility, staying the Crown's claim to the GST funds no longer served a purpose under the *CCAA* and the court was bound under the priority scheme provided by the *ETA* to allow payment to the Crown. In so holding, Tysoe J.A. adopted the reasoning in *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737 (C.A.), which found that the *ETA* deemed trust for GST established Crown priority over secured creditors under the *CCAA*.

8 Second, Tysoe J.A. concluded that by ordering the GST funds segregated in the Monitor's trust account on April 29, 2008, the judge had created an express trust in favour of the Crown from which the monies in question could not be diverted for any other purposes. The Court of Appeal therefore ordered that the money held by the Monitor in trust be paid to the Receiver General.

2. Issues

9 This appeal raises three broad issues which are addressed in turn:

(1) Did s. 222(3) of the *ETA* displace s. 18.3(1) of the *CCAA* and give priority to the Crown's *ETA* deemed trust during *CCAA* proceedings as held in *Ottawa Senators*?
(2) Did the court exceed its *CCAA* authority by lifting the stay to allow the debtor to make an assignment in bankruptcy?
(3) Did the court's order of April 29, 2008 requiring segregation of the Crown's GST claim in the Monitor's trust account create an express trust in favour of the Crown in respect of those funds?

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3. Analysis

10 The first issue concerns Crown priorities in the context of insolvency. As will be seen, the *ETA* provides for a deemed trust in favour of the Crown in respect of GST owed by a debtor "[d]espite ... any other enactment of Canada (except the *Bankruptcy and Insolvency Act*)" (s.

222(3)), while the *CCAA* stated at the relevant time that "notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be [so] regarded" (s. 18.3(1)). It is difficult to imagine two statutory provisions more apparently in conflict. However, as is often the case, the apparent conflict can be resolved through interpretation.

11 In order to properly interpret the provisions, it is necessary to examine the history of the *CCAA*, its function amidst the body of insolvency legislation enacted by Parliament, and the principles that have been recognized in the jurisprudence. It will be seen that Crown priorities in the insolvency context have been significantly pared down. The resolution of the second issue is also rooted in the context of the *CCAA*, but its purpose and the manner in which it has been interpreted in the case law are also key. After examining the first two issues in this case, I will address Tysoe J.A.'s conclusion that an express trust in favour of the Crown was created by the court's order of April 29, 2008.

3.1 *Purpose and Scope of Insolvency Law*

12 Insolvency is the factual situation that arises when a debtor is unable to pay creditors (see generally, R. J. Wood, *Bankruptcy and Insolvency Law* (2009), at p. 16). Certain legal proceedings become available upon insolvency, which typically allow a debtor to obtain a court order staying its creditors' enforcement actions and attempt to obtain [page393] a binding compromise with creditors to adjust the payment conditions to something more realistic. Alternatively, the debtor's assets may be liquidated and debts paid from the proceeds according to statutory priority rules. The former is usually referred to as reorganization or restructuring while the latter is termed liquidation.

13 Canadian commercial insolvency law is not codified in one exhaustive statute. Instead, Parliament has enacted multiple insolvency statutes, the main one being the *BIA*. The *BIA* offers a self-contained legal regime providing for both reorganization and liquidation. Although bankruptcy legislation has a long history, the *BIA* itself is a fairly recent statute -- it was enacted in 1992. It is characterized by a rules-based approach to proceedings. The *BIA* is available to insolvent debtors owing $1000 or more, regardless of whether they are natural or legal persons. It contains mechanisms for debtors to make proposals to their creditors for the adjustment of debts. If a proposal fails, the *BIA* contains a bridge to bankruptcy whereby the debtor's assets are liquidated and the proceeds paid to creditors in accordance with the statutory scheme of distribution.

14 Access to the *CCAA* is more restrictive. A debtor must be a company with liabilities in excess of $5 million. Unlike the *BIA*, the *CCAA* contains no provisions for liquidation of a debtor's assets if reorganization fails. There are three ways of exiting *CCAA* proceedings. The best outcome is achieved when the stay of proceedings provides the debtor with some breathing space during which solvency is restored and the *CCAA* process terminates without reorganization being needed. The second most desirable outcome occurs when the debtor's compromise or arrangement is accepted by its creditors and the reorganized company emerges from the *CCAA* proceedings as a going concern.

Lastly, if the compromise or arrangement fails, either [page394] the company or its creditors usually seek to have the debtor's assets liquidated under the applicable provisions of the *BIA* or to place the debtor into receivership. As discussed in greater detail below, the key difference between the reorganization regimes under the *BIA* and the *CCAA* is that the latter offers a more flexible mechanism with greater judicial discretion, making it more responsive to complex reorganizations.

15 As I will discuss at greater length below, the purpose of the *CCAA* -- Canada's first reorganization statute -- is to permit the debtor to continue to carry on business and, where possible, avoid the social and economic costs of liquidating its assets. Proposals to creditors under the *BIA* serve the same remedial purpose, though this is achieved through a rules-based mechanism that offers less flexibility. Where reorganization is impossible, the *BIA* may be employed to provide an orderly mechanism for the distribution of a debtor's assets to satisfy creditor claims according to predetermined priority rules.

16 Prior to the enactment of the *CCAA* in 1933 (S.C. 1932-33, c. 36), practice under existing commercial insolvency legislation tended heavily towards the liquidation of a debtor company (J. Sarra, *Creditor Rights and the Public Interest: Restructuring Insolvent Corporations* (2003), at p. 12). The battering visited upon Canadian businesses by the Great Depression and the absence of an effective mechanism for reaching a compromise between debtors and creditors to avoid liquidation required a legislative response. The *CCAA* was innovative as it allowed the insolvent debtor to attempt reorganization under judicial supervision outside the existing insolvency legislation which, once engaged, almost invariably resulted in liquidation (*Reference re Companies' Creditors [page395] Arrangement Act*, [1934] S.C.R. 659, at pp. 660-61; Sarra, *Creditor Rights*, at pp. 12-13).

17 Parliament understood when adopting the *CCAA* that liquidation of an insolvent company was harmful for most of those it affected -- notably creditors and employees -- and that a workout which allowed the company to survive was optimal (Sarra, *Creditor Rights*, at pp. 13-15).

18 Early commentary and jurisprudence also endorsed the *CCAA*'s remedial objectives. It recognized that companies retain more value as going concerns while underscoring that intangible losses, such as the evaporation of the companies' goodwill, result from liquidation (S. E. Edwards, "Reorganizations Under the Companies' Creditors Arrangement Act" (1947), 25 *Can. Bar Rev.* 587, at p. 592). Reorganization serves the public interest by facilitating the survival of companies supplying goods or services crucial to the health of the economy or saving large numbers of jobs (*ibid.*, at p. 593). Insolvency could be so widely felt as to impact stakeholders other than creditors and employees. Variants of these views resonate today, with reorganization justified in terms of rehabilitating companies that are key elements in a complex web of interdependent economic relationships in order to avoid the negative consequences of liquidation.

19 The *CCAA* fell into disuse during the next several decades, likely because amendments to the Act in 1953 restricted its use to companies issuing bonds (S.C. 1952-53, c. 3). During the economic

downturn of the early 1980s, insolvency lawyers and courts adapting to the resulting wave of insolvencies resurrected the statute and deployed it in response to new economic challenges. Participants in insolvency proceedings grew to recognize and appreciate the statute's distinguishing feature: a grant of broad and flexible authority to the supervising court to make [page396] the orders necessary to facilitate the reorganization of the debtor and achieve the *CCAA*'s objectives. The manner in which courts have used *CCAA* jurisdiction in increasingly creative and flexible ways is explored in greater detail below.

20 Efforts to evolve insolvency law were not restricted to the courts during this period. In 1970, a government-commissioned panel produced an extensive study recommending sweeping reform but Parliament failed to act (see *Bankruptcy and Insolvency: Report of the Study Committee on Bankruptcy and Insolvency Legislation* (1970)). Another panel of experts produced more limited recommendations in 1986 which eventually resulted in enactment of the *Bankruptcy and Insolvency Act* of 1992 (S.C. 1992, c. 27) (see *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency* (1986)). Broader provisions for reorganizing insolvent debtors were then included in Canada's bankruptcy statute. Although the 1970 and 1986 reports made no specific recommendations with respect to the *CCAA*, the House of Commons committee studying the *BIA*'s predecessor bill, C-22, seemed to accept expert testimony that the *BIA*'s new reorganization scheme would shortly supplant the *CCAA*, which could then be repealed, with commercial insolvency and bankruptcy being governed by a single statute (*Minutes of Proceedings and Evidence of the Standing Committee on Consumer and Corporate Affairs and Government Operations*, Issue No. 15, 3rd Sess., 34th Parl., October 3, 1991, at 15:15-15:16).

21 In retrospect, this conclusion by the House of Commons committee was out of step with reality. It overlooked the renewed vitality the *CCAA* enjoyed in contemporary practice and the advantage that a [page397] flexible judicially supervised reorganization process presented in the face of increasingly complex reorganizations, when compared to the stricter rules-based scheme contained in the *BIA*. The "flexibility of the *CCAA* [was seen as] a great benefit, allowing for creative and effective decisions" (Industry Canada, Marketplace Framework Policy Branch, *Report on the Operation and Administration of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (2002), at p. 41). Over the past three decades, resurrection of the *CCAA* has thus been the mainspring of a process through which, one author concludes, "the legal setting for Canadian insolvency restructuring has evolved from a rather blunt instrument to one of the most sophisticated systems in the developed world" (R. B. Jones, "The Evolution of Canadian Restructuring: Challenges for the Rule of Law", in J. P. Sarra, ed., *Annual Review of Insolvency Law 2005* (2006), 481, at p. 481).

22 While insolvency proceedings may be governed by different statutory schemes, they share some commonalities. The most prominent of these is the single proceeding model. The nature and purpose of the single proceeding model are described by Professor Wood in *Bankruptcy and Insolvency Law*:

> They all provide a collective proceeding that supersedes the usual civil process available to creditors to enforce their claims. The creditors' remedies are collectivized in order to prevent the free-for-all that would otherwise prevail if creditors were permitted to exercise their remedies. In the absence of a collective process, each creditor is armed with the knowledge that if they do not strike hard and swift to seize the debtor's assets, they will be beat out by other creditors. [pp. 2-3]

The single proceeding model avoids the inefficiency and chaos that would attend insolvency if each creditor initiated proceedings to recover its debt. Grouping all possible actions against the debtor into a single proceeding controlled in a single forum facilitates negotiation with creditors because it places them all on an equal footing, [page398] rather than exposing them to the risk that a more aggressive creditor will realize its claims against the debtor's limited assets while the other creditors attempt a compromise. With a view to achieving that purpose, both the *CCAA* and the *BIA* allow a court to order all actions against a debtor to be stayed while a compromise is sought.

23 Another point of convergence of the *CCAA* and the *BIA* relates to priorities. Because the *CCAA* is silent about what happens if reorganization fails, the *BIA* scheme of liquidation and distribution necessarily supplies the backdrop for what will happen if a *CCAA* reorganization is ultimately unsuccessful. In addition, one of the important features of legislative reform of both statutes since the enactment of the *BIA* in 1992 has been a cutback in Crown priorities (S.C. 1992, c. 27, s. 39; S.C. 1997, c. 12, ss. 73 and 125; S.C. 2000, c. 30, s. 148; S.C. 2005, c. 47, ss. 69 and 131; S.C. 2009, c. 33, s. 25; see also *Quebec (Revenue) v. Caisse populaire Desjardins de Montmagny*, 2009 SCC 49, [2009] 3 S.C.R. 286; *Deputy Minister of Revenue v. Rainville*, [1980] 1 S.C.R. 35; *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency*).

24 With parallel *CCAA* and *BIA* restructuring schemes now an accepted feature of the insolvency law landscape, the contemporary thrust of legislative reform has been towards harmonizing aspects of insolvency law common to the two statutory schemes to the extent possible and encouraging reorganization over liquidation (see *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, S.C. 2005, c. 47; *Gauntlet Energy Corp., Re*, 2003 ABQB 894, 30 Alta. L.R. (4th) 192, at para. 19).

25 Mindful of the historical background of the *CCAA* and *BIA*, I now turn to the first question at issue.

[page399]

3.2 *GST Deemed Trust Under the CCAA*

26 The Court of Appeal proceeded on the basis that the *ETA* precluded the court from staying the Crown's enforcement of the GST deemed trust when partially lifting the stay to allow the debtor to enter bankruptcy. In so doing, it adopted the reasoning in a line of cases culminating in *Ottawa Senators*, which held that an *ETA* deemed trust remains enforceable during *CCAA* reorganization despite language in the *CCAA* that suggests otherwise.

27 The Crown relies heavily on the decision of the Ontario Court of Appeal in *Ottawa Senators* and argues that the later in time provision of the *ETA* creating the GST deemed trust trumps the provision of the *CCAA* purporting to nullify most statutory deemed trusts. The Court of Appeal in this case accepted this reasoning but not all provincial courts follow it (see, e.g., *Komunik Corp. (Arrangement relatif à)*, 2009 QCCS 6332 (CanLII), leave to appeal granted, 2010 QCCA 183 (CanLII)). Century Services relied, in its written submissions to this Court, on the argument that the court had authority under the *CCAA* to continue the stay against the Crown's claim for unremitted GST. In oral argument, the question of whether *Ottawa Senators* was correctly decided nonetheless arose. After the hearing, the parties were asked to make further written submissions on this point. As appears evident from the reasons of my colleague Abella J., this issue has become prominent before this Court. In those circumstances, this Court needs to determine the correctness of the reasoning in *Ottawa Senators*.

28 The policy backdrop to this question involves the Crown's priority as a creditor in insolvency situations which, as I mentioned above, has evolved considerably. Prior to the 1990s, Crown claims [page400] largely enjoyed priority in insolvency. This was widely seen as unsatisfactory as shown by both the 1970 and 1986 insolvency reform proposals, which recommended that Crown claims receive no preferential treatment. A closely related matter was whether the *CCAA* was binding at all upon the Crown. Amendments to the *CCAA* in 1997 confirmed that it did indeed bind the Crown (see *CCAA*, s. 21, as added by S.C. 1997, c. 12, s. 126).

29 Claims of priority by the state in insolvency situations receive different treatment across jurisdictions worldwide. For example, in Germany and Australia, the state is given no priority at all, while the state enjoys wide priority in the United States and France (see B. K. Morgan, "Should the Sovereign be Paid First? A Comparative International Analysis of the Priority for Tax Claims in Bankruptcy" (2000), 74 *Am. Bankr. L.J.* 461, at p. 500). Canada adopted a middle course through legislative reform of Crown priority initiated in 1992. The Crown retained priority for source deductions of income tax, Employment Insurance ("EI") and Canada Pension Plan ("CPP") premiums, but ranks as an ordinary unsecured creditor for most other claims.

30 Parliament has frequently enacted statutory mechanisms to secure Crown claims and permit their enforcement. The two most common are statutory deemed trusts and powers to garnish funds third parties owe the debtor (see F. L. Lamer, *Priority of Crown Claims in Insolvency* (loose-leaf), at s.2).

31 With respect to GST collected, Parliament has enacted a deemed trust. The *ETA* states that

every person who collects an amount on account of GST is deemed to hold that amount in trust for the Crown (s. 222(1)). The deemed trust extends to other property of the person collecting the tax equal in value to the amount deemed to be in trust if that amount has not been remitted in accordance with the *ETA*. The deemed trust also extends to property [page401] held by a secured creditor that, but for the security interest, would be property of the person collecting the tax (s. 222(3)).

32 Parliament has created similar deemed trusts using almost identical language in respect of source deductions of income tax, EI premiums and CPP premiums (see s. 227(4) of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) ("*ITA*"), ss. 86(2) and (2.1) of the *Employment Insurance Act*, S.C. 1996, c. 23, and ss. 23(3) and (4) of the *Canada Pension Plan*, R.S.C. 1985, c. C-8). I will refer to income tax, EI and CPP deductions as "source deductions".

33 In *Royal Bank of Canada v. Sparrow Electric Corp.*, [1997] 1 S.C.R. 411, this Court addressed a priority dispute between a deemed trust for source deductions under the *ITA* and security interests taken under both the *Bank Act*, S.C. 1991, c. 46, and the Alberta *Personal Property Security Act*, S.A. 1988, c. P-4.05 ("*PPSA*"). As then worded, an *ITA* deemed trust over the debtor's property equivalent to the amount owing in respect of income tax became effective at the time of liquidation, receivership, or assignment in bankruptcy. *Sparrow Electric* held that the *ITA* deemed trust could not prevail over the security interests because, being fixed charges, the latter attached as soon as the debtor acquired rights in the property such that the *ITA* deemed trust had no property on which to attach when it subsequently arose. Later, in *First Vancouver Finance v. M.N.R.*, 2002 SCC 49, [2002] 2 S.C.R. 720, this Court observed that Parliament had legislated to strengthen the statutory deemed trust in the *ITA* by deeming it to operate from the moment the deductions were not paid to the Crown as required by the *ITA*, and by granting the Crown priority over all security interests (paras. 27-29) (the "*Sparrow Electric* amendment").

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34 The amended text of s. 227(4.1) of the *ITA* and concordant source deductions deemed trusts in the *Canada Pension Plan* and the *Employment Insurance Act* state that the deemed trust operates notwithstanding any other enactment of Canada, except ss. 81.1 and 81.2 of the *BIA*. The *ETA* deemed trust at issue in this case is similarly worded, but it excepts the *BIA* in its entirety. The provision reads as follows:

> **222...** .
>
> ...
>
> (3) Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act*), any

> enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed ... .

35 The Crown submits that the *Sparrow Electric* amendment, added by Parliament to the *ETA* in 2000, was intended to preserve the Crown's priority over collected GST under the *CCAA* while subordinating the Crown to the status of an unsecured creditor in respect of GST only under the *BIA*. This is because the *ETA* provides that the GST deemed trust is effective "despite" any other enactment except the *BIA*.

36 The language used in the *ETA* for the GST deemed trust creates an apparent conflict with the *CCAA*, which provides that subject to certain exceptions, property deemed by statute to be held in trust for the Crown shall not be so regarded.

37 Through a 1997 amendment to the *CCAA* (S.C. 1997, c. 12, s. 125), Parliament appears to have, [page403] subject to specific exceptions, nullified deemed trusts in favour of the Crown once reorganization proceedings are commenced under the Act. The relevant provision reads:

> **18.3** (1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

This nullification of deemed trusts was continued in further amendments to the *CCAA* (S.C. 2005, c. 47), where s. 18.3(1) was renumbered and reformulated as s. 37(1):

> **37.** (1) Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

38 An analogous provision exists in the *BIA*, which, subject to the same specific exceptions, nullifies statutory deemed trusts and makes property of the bankrupt that would otherwise be subject to a deemed trust part of the debtor's estate and available to creditors (S.C. 1992, c. 27, s. 39; S.C. 1997, c. 12, s. 73; *BIA*, s. 67(2)). It is noteworthy that in both the *CCAA* and the *BIA*, the exceptions concern source deductions (*CCAA*, s. 18.3(2); *BIA*, s. 67(3)). The relevant provision of the *CCAA* reads:

> **18.3** ...
>
> (2) Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act*... .

Thus, the Crown's deemed trust and corresponding priority in source deductions remain effective both in reorganization and in bankruptcy.

[page404]

39 Meanwhile, in both s. 18.4(1) of the *CCAA* and s. 86(1) of the *BIA*, other Crown claims are treated as unsecured. These provisions, establishing the Crown's status as an unsecured creditor, explicitly exempt statutory deemed trusts in source deductions (*CCAA*, s. 18.4(3); *BIA*, s. 86(3)). The *CCAA* provision reads as follows:

> **18.4** ...
>
> ...
>
> (3) Subsection (1) [Crown ranking as unsecured creditor] does not affect the operation of
>
> (*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*,
>
> (*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution ... .

Therefore, not only does the *CCAA* provide that Crown claims do not enjoy priority over the claims of other creditors (s. 18.3(1)), but the exceptions to this rule (i.e., that Crown priority is maintained for source deductions) are repeatedly stated in the statute.

40 The apparent conflict in this case is whether the rule in the *CCAA* first enacted as s. 18.3 in 1997, which provides that subject to certain explicit exceptions, statutory deemed trusts are ineffective under the *CCAA*, is overridden by the one in the *ETA* enacted in 2000 stating that GST deemed trusts operate despite any enactment of Canada except the *BIA*. With respect for my colleague Fish J., I do not think the apparent conflict can be resolved by denying it and creating a

rule requiring both a statutory provision enacting the deemed trust, and a second statutory provision confirming it. Such a rule is unknown to the law. Courts must recognize [page405] conflicts, apparent or real, and resolve them when possible.

41 A line of jurisprudence across Canada has resolved the apparent conflict in favour of the *ETA*, thereby maintaining GST deemed trusts under the *CCAA*. *Ottawa Senators*, the leading case, decided the matter by invoking the doctrine of implied repeal to hold that the later in time provision of the *ETA* should take precedence over the *CCAA* (see also *Solid Resources Ltd., Re* (2002), 40 C.B.R. (4th) 219 (Alta. Q.B.); *Gauntlet*).

42 The Ontario Court of Appeal in *Ottawa Senators* rested its conclusion on two considerations. First, it was persuaded that by explicitly mentioning the *BIA* in *ETA* s. 222(3), but not the *CCAA*, Parliament made a deliberate choice. In the words of MacPherson J.A.:

> The *BIA* and the *CCAA* are closely related federal statutes. I cannot conceive that Parliament would specifically identify the *BIA* as an exception, but accidentally fail to consider the *CCAA* as a possible second exception. In my view, the omission of the *CCAA* from s. 222(3) of the *ETA* was almost certainly a considered omission. [para. 43]

43 Second, the Ontario Court of Appeal compared the conflict between the *ETA* and the *CCAA* to that before this Court in *Doré v. Verdun (City)*, [1997] 2 S.C.R. 862, and found them to be "identical" (para. 46). It therefore considered *Doré* binding (para. 49). In *Doré*, a limitations provision in the more general and recently enacted *Civil Code of Québec*, S.Q. 1991, c. 64 ("*C.C.Q.*"), was held to have repealed a more specific provision of the earlier Quebec *Cities and Towns Act*, R.S.Q., c. C-19, with which it conflicted. By analogy, [page406] the Ontario Court of Appeal held that the later in time and more general provision, s. 222(3) of the *ETA*, impliedly repealed the more specific and earlier in time provision, s. 18.3(1) of the *CCAA* (paras. 47-49).

44 Viewing this issue in its entire context, several considerations lead me to conclude that neither the reasoning nor the result in *Ottawa Senators* can stand. While a conflict may exist at the level of the statutes' wording, a purposive and contextual analysis to determine Parliament's true intent yields the conclusion that Parliament could not have intended to restore the Crown's deemed trust priority in GST claims under the *CCAA* when it amended the *ETA* in 2000 with the *Sparrow Electric* amendment.

45 I begin by recalling that Parliament has shown its willingness to move away from asserting priority for Crown claims in insolvency law. Section 18.3(1) of the *CCAA* (subject to the s. 18.3(2) exceptions) provides that the Crown's deemed trusts have no effect under the *CCAA*. Where Parliament has sought to protect certain Crown claims through statutory deemed trusts and intended that these deemed trusts continue in insolvency, it has legislated so explicitly and elaborately. For example, s. 18.3(2) of the *CCAA* and s. 67(3) of the *BIA* expressly provide that deemed trusts for source deductions remain effective in insolvency. Parliament has, therefore, clearly carved out

exceptions from the general rule that deemed trusts are ineffective in insolvency. The *CCAA* and *BIA* are in harmony, preserving deemed trusts and asserting Crown priority only in respect of source deductions. Meanwhile, there is no express statutory basis for concluding that GST claims enjoy a preferred treatment under the *CCAA* or the *BIA*. Unlike source deductions, which are clearly and expressly dealt with under both these insolvency statutes, no such clear and express language exists [page407] in those Acts carving out an exception for GST claims.

46 The internal logic of the *CCAA* also militates against upholding the *ETA* deemed trust for GST. The *CCAA* imposes limits on a suspension by the court of the Crown's rights in respect of source deductions but does not mention the *ETA* (s. 11.4). Since source deductions deemed trusts are granted explicit protection under the *CCAA*, it would be inconsistent to afford a better protection to the *ETA* deemed trust absent explicit language in the *CCAA*. Thus, the logic of the *CCAA* appears to subject the *ETA* deemed trust to the waiver by Parliament of its priority (s. 18.4).

47 Moreover, a strange asymmetry would arise if the interpretation giving the *ETA* priority over the *CCAA* urged by the Crown is adopted here: the Crown would retain priority over GST claims during *CCAA* proceedings but not in bankruptcy. As courts have reflected, this can only encourage statute shopping by secured creditors in cases such as this one where the debtor's assets cannot satisfy both the secured creditors' and the Crown's claims (*Gauntlet*, at para. 21). If creditors' claims were better protected by liquidation under the *BIA*, creditors' incentives would lie overwhelmingly with avoiding proceedings under the *CCAA* and not risking a failed reorganization. Giving a key player in any insolvency such skewed incentives against reorganizing under the *CCAA* can only undermine that statute's remedial objectives and risk inviting the very social ills that it was enacted to avert.

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48 Arguably, the effect of *Ottawa Senators* is mitigated if restructuring is attempted under the *BIA* instead of the *CCAA*, but it is not cured. If *Ottawa Senators* were to be followed, Crown priority over GST would differ depending on whether restructuring took place under the *CCAA* or the *BIA*. The anomaly of this result is made manifest by the fact that it would deprive companies of the option to restructure under the more flexible and responsive *CCAA* regime, which has been the statute of choice for complex reorganizations.

49 Evidence that Parliament intended different treatments for GST claims in reorganization and bankruptcy is scant, if it exists at all. Section 222(3) of the *ETA* was enacted as part of a wide-ranging budget implementation bill in 2000. The summary accompanying that bill does not indicate that Parliament intended to elevate Crown priority over GST claims under the *CCAA* to the same or a higher level than source deductions claims. Indeed, the summary for deemed trusts states only that amendments to existing provisions are aimed at "ensuring that employment insurance

premiums and Canada Pension Plan contributions that are required to be remitted by an employer are fully recoverable by the Crown in the case of the bankruptcy of the employer" (Summary to S.C. 2000, c. 30, at p. 4a). The wording of GST deemed trusts resembles that of statutory deemed trusts for source deductions and incorporates the same overriding language and reference to the *BIA*. However, as noted above, Parliament's express intent is that only source deductions deemed trusts remain operative. An exception for the *BIA* in the statutory language establishing the source deductions deemed trusts accomplishes very little, because the explicit language of the *BIA* itself (and the *CCAA*) carves out these source deductions deemed trusts and maintains their effect. It is however noteworthy that no equivalent language maintaining GST deemed trusts exists under either the *BIA* or the *CCAA*.

[page409]

50 It seems more likely that by adopting the same language for creating GST deemed trusts in the *ETA* as it did for deemed trusts for source deductions, and by overlooking the inclusion of an exception for the *CCAA* alongside the *BIA* in s. 222(3) of the *ETA*, Parliament may have inadvertently succumbed to a drafting anomaly. Because of a statutory lacuna in the *ETA*, the GST deemed trust could be seen as remaining effective in the *CCAA*, while ceasing to have any effect under the *BIA*, thus creating an apparent conflict with the wording of the *CCAA*. However, it should be seen for what it is: a facial conflict only, capable of resolution by looking at the broader approach taken to Crown priorities and by giving precedence to the statutory language of s. 18.3 of the *CCAA* in a manner that does not produce an anomalous outcome.

51 Section 222(3) of the *ETA* evinces no explicit intention of Parliament to repeal *CCAA* s. 18.3. It merely creates an apparent conflict that must be resolved by statutory interpretation. Parliament's intent when it enacted *ETA* s. 222(3) was therefore far from unambiguous. Had it sought to give the Crown a priority for GST claims, it could have done so explicitly as it did for source deductions. Instead, one is left to infer from the language of *ETA* s. 222(3) that the GST deemed trust was intended to be effective under the *CCAA*.

52 I am not persuaded that the reasoning in *Doré* requires the application of the doctrine of implied repeal in the circumstances of this case. The main issue in *Doré* concerned the impact of the adoption of the *C.C.Q.* on the administrative law rules with respect to municipalities. While Gonthier J. concluded in that case that the limitation provision in art. 2930 *C.C.Q.* had repealed by implication a limitation provision in the *Cities and Towns Act*, he did so on the basis of more than a textual analysis. The conclusion in *Doré* was reached after thorough [page410] contextual analysis of both pieces of legislation, including an extensive review of the relevant legislative history (paras. 31-41). Consequently, the circumstances before this Court in *Doré* are far from "identical" to those in the present case, in terms of text, context and legislative history. Accordingly, *Doré* cannot be said to require the automatic application of the rule of repeal by implication.

53 A noteworthy indicator of Parliament's overall intent is the fact that in subsequent amendments it has not displaced the rule set out in the *CCAA*. Indeed, as indicated above, the recent amendments to the *CCAA* in 2005 resulted in the rule previously found in s. 18.3 being renumbered and reformulated as s. 37. Thus, to the extent the interpretation allowing the GST deemed trust to remain effective under the *CCAA* depends on *ETA* s. 222(3) having impliedly repealed *CCAA* s. 18.3(1) because it is later in time, we have come full circle. Parliament has renumbered and reformulated the provision of the *CCAA* stating that, subject to exceptions for source deductions, deemed trusts do not survive the *CCAA* proceedings and thus the *CCAA* is now the later in time statute. This confirms that Parliament's intent with respect to GST deemed trusts is to be found in the *CCAA*.

54 I do not agree with my colleague Abella J. that s. 44(*f*) of the *Interpretation Act*, R.S.C. 1985, c. I-21, can be used to interpret the 2005 amendments as having no effect. The new statute can hardly be said to be a mere re-enactment of the former statute. Indeed, the *CCAA* underwent a substantial review in 2005. Notably, acting consistently with its goal of treating both the *BIA* and the *CCAA* as sharing the same approach to insolvency, Parliament made parallel amendments to both statutes with respect to corporate proposals. In addition, new provisions were introduced regarding [page411] the treatment of contracts, collective agreements, interim financing and governance agreements. The appointment and role of the Monitor was also clarified. Noteworthy are the limits imposed by *CCAA* s. 11.09 on the court's discretion to make an order staying the Crown's source deductions deemed trusts, which were formerly found in s. 11.4. No mention whatsoever is made of GST deemed trusts (see Summary to S.C. 2005, c. 47). The review went as far as looking at the very expression used to describe the statutory override of deemed trusts. The comments cited by my colleague only emphasize the clear intent of Parliament to maintain its policy that only source deductions deemed trusts survive in *CCAA* proceedings.

55 In the case at bar, the legislative context informs the determination of Parliament's legislative intent and supports the conclusion that *ETA* s. 222(3) was not intended to narrow the scope of the *CCAA*'s override provision. Viewed in its entire context, the conflict between the *ETA* and the *CCAA* is more apparent than real. I would therefore not follow the reasoning in *Ottawa Senators* and affirm that *CCAA* s. 18.3 remained effective.

56 My conclusion is reinforced by the purpose of the *CCAA* as part of Canadian remedial insolvency legislation. As this aspect is particularly relevant to the second issue, I will now discuss how courts have interpreted the scope of their discretionary powers in supervising a *CCAA* reorganization and how Parliament has largely endorsed this interpretation. Indeed, the interpretation courts have given to the *CCAA* helps in understanding how the *CCAA* grew to occupy such a prominent role in Canadian insolvency law.

[page412]

3.3 *Discretionary Power of a Court Supervising a CCAA Reorganization*

57 Courts frequently observe that "[t]he *CCAA* is skeletal in nature" and does not "contain a comprehensive code that lays out all that is permitted or barred" (*Metcalfe & Mansfield Alternative Investments II Corp. (Re)*, 2008 ONCA 587, 92 O.R. (3d) 513, at para. 44, *per* Blair J.A.). Accordingly, "[t]he history of CCAA law has been an evolution of judicial interpretation" (*Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106 (Ont. Ct. (Gen. Div.)), at para. 10, *per* Farley J.).

58 *CCAA* decisions are often based on discretionary grants of jurisdiction. The incremental exercise of judicial discretion in commercial courts under conditions one practitioner aptly describes as "the hothouse of real-time litigation" has been the primary method by which the *CCAA* has been adapted and has evolved to meet contemporary business and social needs (see Jones, at p. 484).

59 Judicial discretion must of course be exercised in furtherance of the *CCAA*'s purposes. The remedial purpose I referred to in the historical overview of the Act is recognized over and over again in the jurisprudence. To cite one early example:

> The legislation is remedial in the purest sense in that it provides a means whereby the devastating social and economic effects of bankruptcy or creditor initiated termination of ongoing business operations can be avoided while a court-supervised attempt to reorganize the financial affairs of the debtor company is made.
>
> (*Elan Corp. v. Comiskey* (1990), 41 O.A.C. 282 , at para. 57, *per* Doherty J.A., dissenting)

60 Judicial decision making under the *CCAA* takes many forms. A court must first of all provide the conditions under which the debtor can attempt to reorganize. This can be achieved by [page413] staying enforcement actions by creditors to allow the debtor's business to continue, preserving the *status quo* while the debtor plans the compromise or arrangement to be presented to creditors, and supervising the process and advancing it to the point where it can be determined whether it will succeed (see, e.g., *Chef Ready Foods Ltd. v. Hongkong Bank of Can.* (1990), 51 B.C.L.R. (2d) 84 (C.A.), at pp. 88-89; *Pacific National Lease Holding Corp., Re* (1992), 19 B.C.A.C. 134, at para. 27). In doing so, the court must often be cognizant of the various interests at stake in the reorganization, which can extend beyond those of the debtor and creditors to include employees, directors, shareholders, and even other parties doing business with the insolvent company (see, e.g., *Canadian Airlines Corp., Re*, 2000 ABQB 442, 84 Alta. L.R. (3d) 9, at para. 144, *per* Paperny J. (as she then was); *Air Canada, Re* (2003), 42 C.B.R. (4th) 173 (Ont. S.C.J.), at para. 3; *Air Canada, Re*, 2003 CanLII 49366 (Ont. S.C.J.), at para. 13, *per* Farley J.; Sarra, *Creditor Rights*, at pp. 181-92 and 217-26). In addition, courts must recognize that on occasion the broader public interest will be engaged by aspects of the reorganization and may be a factor against which the decision of whether to allow a particular action will be weighed (see, e.g., *Canadian Red Cross Society/Société*

Canadienne de la Croix Rouge, Re (2000), 19 C.B.R. (4th) 158 (Ont. S.C.J.), at para. 2, *per* Blair J. (as he then was); Sarra, *Creditor Rights*, at pp. 195-214).

61 When large companies encounter difficulty, reorganizations become increasingly complex. *CCAA* courts have been called upon to innovate accordingly in exercising their jurisdiction beyond merely staying proceedings against the debtor to allow breathing room for reorganization. They have been asked to sanction measures for which there is no explicit authority in the *CCAA*. Without exhaustively cataloguing the various measures taken under the authority of the *CCAA*, it is useful to refer briefly to a few examples to illustrate the flexibility the statute affords supervising courts.

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62 Perhaps the most creative use of *CCAA* authority has been the increasing willingness of courts to authorize post-filing security for debtor in possession financing or super-priority charges on the debtor's assets when necessary for the continuation of the debtor's business during the reorganization (see, e.g., *Skydome Corp., Re* (1998), 16 C.B.R. (4th) 118 (Ont. Ct. (Gen. Div.)); *United Used Auto & Truck Parts Ltd., Re*, 2000 BCCA 146, 135 B.C.A.C. 96, aff'g (1999), 12 C.B.R. (4th) 144 (S.C.); and generally, J. P. Sarra, *Rescue! The Companies' Creditors Arrangement Act* (2007), at pp. 93-115). The *CCAA* has also been used to release claims against third parties as part of approving a comprehensive plan of arrangement and compromise, even over the objections of some dissenting creditors (see *Metcalfe & Mansfield*). As well, the appointment of a Monitor to oversee the reorganization was originally a measure taken pursuant to the *CCAA*'s supervisory authority; Parliament responded, making the mechanism mandatory by legislative amendment.

63 Judicial innovation during *CCAA* proceedings has not been without controversy. At least two questions it raises are directly relevant to the case at bar: (1) What are the sources of a court's authority during *CCAA* proceedings? (2) What are the limits of this authority?

64 The first question concerns the boundary between a court's statutory authority under the *CCAA* and a court's residual authority under its inherent and equitable jurisdiction when supervising a reorganization. In authorizing measures during *CCAA* proceedings, courts have on occasion purported to rely upon their equitable jurisdiction to advance the purposes of the Act or their inherent jurisdiction to fill gaps in the statute. Recent appellate decisions have counselled against [page415] purporting to rely on inherent jurisdiction, holding that the better view is that courts are in most cases simply construing the authority supplied by the *CCAA* itself (see, e.g., *Skeena Cellulose Inc., Re*, 2003 BCCA 344, 13 B.C.L.R. (4th) 236, at paras. 45-47, *per* Newbury J.A.; *Stelco Inc. (Re)* (2005), 75 O.R. (3d) 5 (C.A.), at paras. 31-33, *per* Blair J.A.).

65 I agree with Justice Georgina R. Jackson and Professor Janis Sarra that the most appropriate approach is a hierarchical one in which courts rely first on an interpretation of the provisions of the *CCAA* text before turning to inherent or equitable jurisdiction to anchor measures taken in a *CCAA*

proceeding (see G. R. Jackson and J. Sarra, "Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters", in J. P. Sarra, ed., *Annual Review of Insolvency Law 2007* (2008), 41, at p. 42). The authors conclude that when given an appropriately purposive and liberal interpretation, the *CCAA* will be sufficient in most instances to ground measures necessary to achieve its objectives (p. 94).

66 Having examined the pertinent parts of the *CCAA* and the recent history of the legislation, I accept that in most instances the issuance of an order during *CCAA* proceedings should be considered an exercise in statutory interpretation. Particularly noteworthy in this regard is the expansive interpretation the language of the statute at issue is capable of supporting.

67 The initial grant of authority under the *CCAA* empowered a court "where an application is made under this Act in respect of a company ... on the application of any person interested in the [page416] matter, ... subject to this Act, [to] make an order under this section" (*CCAA*, s. 11(1)). The plain language of the statute was very broad.

68 In this regard, though not strictly applicable to the case at bar, I note that Parliament has in recent amendments changed the wording contained in s. 11(1), making explicit the discretionary authority of the court under the *CCAA*. Thus, in s. 11 of the *CCAA* as currently enacted, a court may, "subject to the restrictions set out in this Act, ... make any order that it considers appropriate in the circumstances" (S.C. 2005, c. 47, s. 128). Parliament appears to have endorsed the broad reading of *CCAA* authority developed by the jurisprudence.

69 The *CCAA* also explicitly provides for certain orders. Both an order made on an initial application and an order on subsequent applications may stay, restrain, or prohibit existing or new proceedings against the debtor. The burden is on the applicant to satisfy the court that the order is appropriate in the circumstances and that the applicant has been acting in good faith and with due diligence (*CCAA*, ss. 11(3), (4) and (6)).

70 The general language of the *CCAA* should not be read as being restricted by the availability of more specific orders. However, the requirements of appropriateness, good faith, and due diligence are baseline considerations that a court should always bear in mind when exercising *CCAA* authority. Appropriateness under the *CCAA* is assessed by inquiring whether the order sought advances the policy objectives underlying the *CCAA*. The question is whether the order will usefully further efforts to achieve the remedial purpose of the *CCAA* -- avoiding the social and economic losses resulting from liquidation of an insolvent company. I would add that appropriateness extends not only to the purpose of the order, but also to the means it employs. Courts should be mindful that chances for successful reorganizations are enhanced where participants achieve common ground and all [page417] stakeholders are treated as advantageously and fairly as the circumstances permit.

71 It is well established that efforts to reorganize under the *CCAA* can be terminated and the stay

of proceedings against the debtor lifted if the reorganization is "doomed to failure" (see *Chef Ready*, at p. 88; *Philip's Manufacturing Ltd., Re* (1992), 9 C.B.R. (3d) 25 (B.C.C.A.), at paras. 6-7). However, when an order is sought that does realistically advance the *CCAA*'s purposes, the ability to make it is within the discretion of a *CCAA* court.

72 The preceding discussion assists in determining whether the court had authority under the *CCAA* to continue the stay of proceedings against the Crown once it was apparent that reorganization would fail and bankruptcy was the inevitable next step.

73 In the Court of Appeal, Tysoe J.A. held that no authority existed under the *CCAA* to continue staying the Crown's enforcement of the GST deemed trust once efforts at reorganization had come to an end. The appellant submits that in so holding, Tysoe J.A. failed to consider the underlying purpose of the *CCAA* and give the statute an appropriately purposive and liberal interpretation under which the order was permissible. The Crown submits that Tysoe J.A. correctly held that the mandatory language of the *ETA* gave the court no option but to permit enforcement of the GST deemed trust when lifting the *CCAA* stay to permit the debtor to make an assignment under the *BIA*. Whether the *ETA* has a mandatory effect in the context of a *CCAA* proceeding has already been discussed. I will now address the question of whether the order was authorized by the *CCAA*.

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74 It is beyond dispute that the *CCAA* imposes no explicit temporal limitations upon proceedings commenced under the Act that would prohibit ordering a continuation of the stay of the Crown's GST claims while lifting the general stay of proceedings temporarily to allow the debtor to make an assignment in bankruptcy.

75 The question remains whether the order advanced the underlying purpose of the *CCAA*. The Court of Appeal held that it did not because the reorganization efforts had come to an end and the *CCAA* was accordingly spent. I disagree.

76 There is no doubt that had reorganization been commenced under the *BIA* instead of the *CCAA*, the Crown's deemed trust priority for the GST funds would have been lost. Similarly, the Crown does not dispute that under the scheme of distribution in bankruptcy under the *BIA* the deemed trust for GST ceases to have effect. Thus, after reorganization under the *CCAA* failed, creditors would have had a strong incentive to seek immediate bankruptcy and distribution of the debtor's assets under the *BIA*. In order to conclude that the discretion does not extend to partially lifting the stay in order to allow for an assignment in bankruptcy, one would have to assume a gap between the *CCAA* and the *BIA* proceedings. Brenner C.J.S.C.'s order staying Crown enforcement of the GST claim ensured that creditors would not be disadvantaged by the attempted reorganization under the *CCAA*. The effect of his order was to blunt any impulse of creditors to interfere in an orderly liquidation. His order was thus in furtherance of the *CCAA*'s objectives to the extent that it

allowed a bridge between the *CCAA* and *BIA* proceedings. This interpretation of the tribunal's discretionary power is buttressed by s. 20 of the *CCAA*. That section provides that the *CCAA* "may be applied together with the provisions of any Act of Parliament ... that authorizes or makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them", such as [page419] the *BIA*. Section 20 clearly indicates the intention of Parliament for the *CCAA* to operate *in tandem* with other insolvency legislation, such as the *BIA*.

77 The *CCAA* creates conditions for preserving the *status quo* while attempts are made to find common ground amongst stakeholders for a reorganization that is fair to all. Because the alternative to reorganization is often bankruptcy, participants will measure the impact of a reorganization against the position they would enjoy in liquidation. In the case at bar, the order fostered a harmonious transition between reorganization and liquidation while meeting the objective of a single collective proceeding that is common to both statutes.

78 Tysoe J.A. therefore erred in my view by treating the *CCAA* and the *BIA* as distinct regimes subject to a temporal gap between the two, rather than as forming part of an integrated body of insolvency law. Parliament's decision to maintain two statutory schemes for reorganization, the *BIA* and the *CCAA*, reflects the reality that reorganizations of differing complexity require different legal mechanisms. By contrast, only one statutory scheme has been found to be needed to liquidate a bankrupt debtor's estate. The transition from the *CCAA* to the *BIA* may require the partial lifting of a stay of proceedings under the *CCAA* to allow commencement of the *BIA* proceedings. However, as Laskin J.A. for the Ontario Court of Appeal noted in a similar competition between secured creditors and the Ontario Superintendent of Financial Services seeking to enforce a deemed trust, "[t]he two statutes are related" and no "gap" exists between the two statutes which would allow the enforcement of property interests at the conclusion of *CCAA* proceedings that would be [page420] lost in bankruptcy (*Ivaco Inc. (Re)* (2006), 83 O.R. (3d) 108, at paras. 62-63).

79 The Crown's priority in claims pursuant to source deductions deemed trusts does not undermine this conclusion. Source deductions deemed trusts survive under both the *CCAA* and the *BIA*. Accordingly, creditors' incentives to prefer one Act over another will not be affected. While a court has a broad discretion to stay source deductions deemed trusts in the *CCAA* context, this discretion is nevertheless subject to specific limitations applicable only to source deductions deemed trusts (*CCAA*, s. 11.4). Thus, if *CCAA* reorganization fails (e.g., either the creditors or the court refuse a proposed reorganization), the Crown can immediately assert its claim in unremitted source deductions. But this should not be understood to affect a seamless transition into bankruptcy or create any "gap" between the *CCAA* and the *BIA* for the simple reason that, regardless of what statute the reorganization had been commenced under, creditors' claims in both instances would have been subject to the priority of the Crown's source deductions deemed trust.

80 Source deductions deemed trusts aside, the comprehensive and exhaustive mechanism under the *BIA* must control the distribution of the debtor's assets once liquidation is inevitable. Indeed, an orderly transition to liquidation is mandatory under the *BIA* where a proposal is rejected by

creditors. The *CCAA* is silent on the transition into liquidation but the breadth of the court's discretion under the Act is sufficient to construct a bridge to liquidation under the *BIA*. The court must do so in a manner that does not subvert the scheme of distribution under the *BIA*. Transition [page421] to liquidation requires partially lifting the *CCAA* stay to commence proceedings under the *BIA*. This necessary partial lifting of the stay should not trigger a race to the courthouse in an effort to obtain priority unavailable under the *BIA*.

81 I therefore conclude that Brenner C.J.S.C. had the authority under the *CCAA* to lift the stay to allow entry into liquidation.

3.4 *Express Trust*

82 The last issue in this case is whether Brenner C.J.S.C. created an express trust in favour of the Crown when he ordered on April 29, 2008, that proceeds from the sale of LeRoy Trucking's assets equal to the amount of unremitted GST be held back in the Monitor's trust account until the results of the reorganization were known. Tysoe J.A. in the Court of Appeal concluded as an alternative ground for allowing the Crown's appeal that it was the beneficiary of an express trust. I disagree.

83 Creation of an express trust requires the presence of three certainties: intention, subject matter, and object. Express or "true trusts" arise from the acts and intentions of the settlor and are distinguishable from other trusts arising by operation of law (see D. W. M. Waters, M. R. Gillen and L. D. Smith, eds., *Waters' Law of Trusts in Canada* (3rd ed. 2005), at pp. 28-29, especially fn. 42).

84 Here, there is no certainty to the object (i.e. the beneficiary) inferrable from the court's order of April 29, 2008 sufficient to support an express trust.

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85 At the time of the order, there was a dispute between Century Services and the Crown over part of the proceeds from the sale of the debtor's assets. The court's solution was to accept LeRoy Trucking's proposal to segregate those monies until that dispute could be resolved. Thus, there was no certainty that the Crown would actually be the beneficiary, or object, of the trust.

86 The fact that the location chosen to segregate those monies was the Monitor's trust account has no independent effect such that it would overcome the lack of a clear beneficiary. In any event, under the interpretation of *CCAA* s. 18.3(1) established above, no such priority dispute would even arise because the Crown's deemed trust priority over GST claims would be lost under the *CCAA* and the Crown would rank as an unsecured creditor for this amount. However, Brenner C.J.S.C. may well have been proceeding on the basis that, in accordance with *Ottawa Senators*, the Crown's GST claim would remain effective if reorganization was successful, which would not be the case if

transition to the liquidation process of the *BIA* was allowed. An amount equivalent to that claim would accordingly be set aside pending the outcome of reorganization.

87 Thus, uncertainty surrounding the outcome of the *CCAA* restructuring eliminates the existence of any certainty to permanently vest in the Crown a beneficial interest in the funds. That much is clear from the oral reasons of Brenner C.J.S.C. on April 29, 2008, when he said: "Given the fact that [*CCAA* proceedings] are known to fail and filings in bankruptcy result, it seems to me that maintaining the status quo in the case at bar supports the proposal to have the monitor hold these funds in trust." Exactly who might take the money in the final result was therefore evidently in doubt. Brenner C.J.S.C.'s subsequent order of September 3, 2008 denying the Crown's application to enforce the trust once it was clear [page423] that bankruptcy was inevitable, confirms the absence of a clear beneficiary required to ground an express trust.

4. Conclusion

88 I conclude that Brenner C.J.S.C. had the discretion under the *CCAA* to continue the stay of the Crown's claim for enforcement of the GST deemed trust while otherwise lifting it to permit LeRoy Trucking to make an assignment in bankruptcy. My conclusion that s. 18.3(1) of the *CCAA* nullified the GST deemed trust while proceedings under that Act were pending confirms that the discretionary jurisdiction under s. 11 utilized by the court was not limited by the Crown's asserted GST priority, because there is no such priority under the *CCAA*.

89 For these reasons, I would allow the appeal and declare that the $305,202.30 collected by LeRoy Trucking in respect of GST but not yet remitted to the Receiver General of Canada is not subject to deemed trust or priority in favour of the Crown. Nor is this amount subject to an express trust. Costs are awarded for this appeal and the appeal in the court below.

The following are the reasons delivered by

FISH J. --

I

90 I am in general agreement with the reasons of Justice Deschamps and would dispose of the appeal as she suggests.

91 More particularly, I share my colleague's interpretation of the scope of the judge's discretion under s. 11 of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). [page424] And I share my colleague's conclusion that Brenner C.J.S.C. did not create an express trust in favour of the Crown when he segregated GST funds into the Monitor's trust account (2008 BCSC 1805, [2008] G.S.T.C. 221).

92 I nonetheless feel bound to add brief reasons of my own regarding the interaction between the *CCAA* and the *Excise Tax Act*, R.S.C. 1985, c. E-15 ("*ETA*").

93 In upholding deemed trusts created by the *ETA* notwithstanding insolvency proceedings, *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737 (C.A.), and its progeny have been unduly protective of Crown interests which Parliament itself has chosen to subordinate to competing prioritized claims. In my respectful view, a clearly marked departure from that jurisprudential approach is warranted in this case.

94 Justice Deschamps develops important historical and policy reasons in support of this position and I have nothing to add in that regard. I do wish, however, to explain why a comparative analysis of related statutory provisions adds support to our shared conclusion.

95 Parliament has in recent years given detailed consideration to the Canadian insolvency scheme. It has declined to amend the provisions at issue in this case. Ours is not to wonder why, but rather to treat Parliament's preservation of the relevant provisions as a deliberate exercise of the legislative discretion that is Parliament's alone. With respect, I reject any suggestion that we should instead characterize the apparent conflict between s. 18.3(1) (now s. 37(1)) of the *CCAA* and s. 222 of the *ETA* as a drafting anomaly or statutory lacuna properly subject to judicial correction or repair.

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II

96 In the context of the Canadian insolvency regime, a deemed trust will be found to exist only where two complementary elements co-exist: first, a statutory provision *creating* the trust; and second, a *CCAA* or *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*") provision *confirming* -- or explicitly preserving -- its effective operation.

97 This interpretation is reflected in three federal statutes. Each contains a deemed trust provision framed in terms strikingly similar to the wording of s. 222 of the *ETA*.

98 The first is the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) ("*ITA*"), where s. 227(4) *creates* a deemed trust:

> (4) Every person who deducts or withholds an amount under this Act is deemed, notwithstanding any security interest (as defined in subsection 224(1.3)) in the amount so deducted or withheld, to hold the amount separate and apart from the property of the person and from property held by any secured creditor (as defined in subsection 224(1.3)) of that person that but for the security interest would be property of the person, in trust for Her Majesty and for payment to Her Majesty in the manner and at the time provided under this Act. [Here and below, the emphasis is of course my own.]

99 In the next subsection, Parliament has taken care to make clear that this trust is unaffected by federal or provincial legislation to the contrary:

> (4.1) Notwithstanding any other provision of this Act, the *Bankruptcy and Insolvency Act* (except sections 81.1 and 81.2 of that Act), any other enactment of Canada, any enactment of a province or any other law, where at any time an amount deemed by subsection 227(4) to be held by a person in trust for Her Majesty is not paid to Her Majesty in the manner and at the time provided under this Act, property of the person ... equal in value to the amount so deemed to be held in trust is deemed
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> (*a*) to be held, from the time the amount was deducted or withheld by the person, separate and [page426] apart from the property of the person, in trust for Her Majesty whether or not the property is subject to such a security interest, ...
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> ...
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> ... and the proceeds of such property shall be paid to the Receiver General in priority to all such security interests.

100 The continued operation of this deemed trust is expressly *confirmed* in s. 18.3 of the *CCAA*:

> **18.3** (1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.
>
> (2) Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* ... .

101 The operation of the *ITA* deemed trust is also confirmed in s. 67 of the *BIA*:

> (2) Subject to subsection (3), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a bankrupt shall not be regarded as held in trust for Her Majesty for the purpose of paragraph (1)(*a*) unless it would be so regarded in the absence of that statutory provision.

> (3) Subsection (2) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* ... .

102 Thus, Parliament has first *created* and then *confirmed the continued operation of* the Crown's *ITA* deemed trust under *both* the *CCAA* and the *BIA* regimes.

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103 The second federal statute for which this scheme holds true is the *Canada Pension Plan*, R.S.C. 1985, c. C-8 ("*CPP*"). At s. 23, Parliament creates a deemed trust in favour of the Crown and specifies that it exists despite all contrary provisions in any other Canadian statute. Finally, and in almost identical terms, the *Employment Insurance Act*, S.C. 1996, c. 23 ("*EIA*"), creates a deemed trust in favour of the Crown: see ss. 86(2) and (2.1).

104 As we have seen, the survival of the deemed trusts created under these provisions of the *ITA*, the *CPP* and the *EIA* is confirmed in s. 18.3(2) of the *CCAA* and in s. 67(3) of the *BIA*. In all three cases, Parliament's intent to enforce the Crown's deemed trust through insolvency proceedings is expressed in clear and unmistakable terms.

105 The same is not true with regard to the deemed trust created under the *ETA*. Although Parliament creates a deemed trust in favour of the Crown to hold unremitted GST monies, and although it purports to maintain this trust notwithstanding any contrary federal or provincial legislation, it does not *confirm* the trust -- or expressly provide for its continued operation -- in either the *BIA* or the *CCAA*. The second of the two mandatory elements I have mentioned is thus absent reflecting Parliament's intention to allow the deemed trust to lapse with the commencement of insolvency proceedings.

106 The language of the relevant *ETA* provisions is identical in substance to that of the *ITA*, *CPP*, and *EIA* provisions:

> **222.** (1) Subject to subsection (1.1), every person who collects an amount as or on account of tax under Division II is deemed, for all purposes and despite any security interest in the amount, to hold the amount in trust for Her Majesty in right of Canada, separate and apart from the property of the person and from property held by any secured creditor of the person that, but for a [page428] security interest, would be property of the person, until the amount is remitted to the Receiver General or withdrawn under subsection (2).

...

> (3) Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and InsolvencyAct*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed
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> > (*a*) to be held, from the time the amount was collected by the person, in trust for Her Majesty, separate and apart from the property of the person, whether or not the property is subject to a security interest, ...
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> > ...
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> ... and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

107 Yet no provision of the *CCAA* provides for the continuation of this deemed trust after the *CCAA* is brought into play.

108 In short, Parliament has imposed *two* explicit conditions, or "building blocks", for survival under the *CCAA* of deemed trusts created by the *ITA*, *CPP*, and *EIA*. Had Parliament intended to likewise preserve under the *CCAA* deemed trusts created by the *ETA*, it would have included in the *CCAA* the sort of confirmatory provision that explicitly preserves other deemed trusts.

109 With respect, unlike Tysoe J.A., I do not find it "inconceivable that Parliament would specifically identify the *BIA* as an exception when enacting the current version of s. 222(3) of the *ETA* without considering the *CCAA* as a possible second exception" (2009 BCCA 205, 98 B.C.L.R. (4th) 242, at para. 37). *All* of the deemed trust [page429] provisions excerpted above make explicit reference to the *BIA*. Section 222 of the *ETA* does not break the pattern. Given the near-identical wording of the four deemed trust provisions, it would have been surprising indeed had Parliament not addressed the *BIA* at all in the *ETA*.

110 Parliament's evident intent was to render GST deemed trusts inoperative upon the institution of insolvency proceedings. Accordingly, s. 222 mentions the *BIA* so as to *exclude* it from its ambit -- rather than to *include* it, as do the *ITA*, the *CPP*, and the *EIA*.

111 Conversely, I note that *none* of these statutes mentions the *CCAA* expressly. Their specific reference to the *BIA* has no bearing on their interaction with the *CCAA*. Again, it is the confirmatory

provisions *in the insolvency statutes* that determine whether a given deemed trust will subsist during insolvency proceedings.

112 Finally, I believe that chambers judges should not segregate GST monies into the Monitor's trust account during *CCAA* proceedings, as was done in this case. The result of Justice Deschamps's reasoning is that GST claims become unsecured under the *CCAA*. Parliament has deliberately chosen to nullify certain Crown super-priorities during insolvency; this is one such instance.

III

113 For these reasons, like Justice Deschamps, I would allow the appeal with costs in this Court and in the courts below and order that the $305,202.30 collected by LeRoy Trucking in respect of GST but not yet remitted to the Receiver General of Canada [page430] be subject to no deemed trust or priority in favour of the Crown.

The following are the reasons delivered by

114 ABELLA J. (dissenting):-- The central issue in this appeal is whether s. 222 of the *Excise Tax Act*, R.S.C. 1985, c. E-15 ("*ETA*"), and specifically s. 222(3), gives priority during *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"), proceedings to the Crown's deemed trust in unremitted GST. I agree with Tysoe J.A. that it does. It follows, in my respectful view, that a court's discretion under s. 11 of the *CCAA* is circumscribed accordingly.

115 Section 11[1] of the *CCAA* stated:

> **11.** (1) Notwithstanding anything in the *Bankruptcy and Insolvency Act* or the *Winding-up Act*, where an application is made under this Act in respect of a company, the court, on the application of any person interested in the matter, may, subject to this Act, on notice to any other person or without notice as it may see fit, make an order under this section.

To decide the scope of the court's discretion under s. 11, it is necessary to first determine the priority issue. Section 222(3), the provision of the *ETA* at issue in this case, states:

[page431]

> (3) Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to

> the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed
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> > (*a*) to be held, from the time the amount was collected by the person, in trust for Her Majesty, separate and apart from the property of the person, whether or not the property is subject to a security interest, and
> >
> > (*b*) to form no part of the estate or property of the person from the time the amount was collected, whether or not the property has in fact been kept separate and apart from the estate or property of the person and whether or not the property is subject to a security interest
>
> and is property beneficially owned by Her Majesty in right of Canada despite any security interest in the property or in the proceeds thereof and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

116 Century Services argued that the *CCAA*'s general override provision, s. 18.3(1), prevailed, and that the deeming provisions in s. 222 of the *ETA* were, accordingly, inapplicable during *CCAA* proceedings. Section 18.3(1) states:

> **18.3** (1) ... [N]otwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

117 As MacPherson J.A. correctly observed in *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737 (C.A.), s. 222(3) of the *ETA* is in "clear conflict" with s. 18.3(1) of the *CCAA* (para. 31). Resolving the conflict between the two provisions is, essentially, what seems to me to be a relatively uncomplicated exercise in statutory [page432] interpretation: Does the language reflect a clear legislative intention? In my view it does. The deemed trust provision, s. 222(3) of the *ETA*, has unambiguous language stating that it operates notwithstanding any law except the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*").

118 By expressly excluding only one statute from its legislative grasp, and by unequivocally stating that it applies despite any other law anywhere in Canada *except* the *BIA*, s. 222(3) has defined its boundaries in the clearest possible terms. I am in complete agreement with the following comments of MacPherson J.A. in *Ottawa Senators*:

> The legislative intent of s. 222(3) of the *ETA* is clear. If there is a conflict with "any other enactment of Canada (except the *Bankruptcy and Insolvency Act*)", s. 222(3) prevails. In these words Parliament did two things: it decided that s. 222(3) should trump all other federal laws and, importantly, it addressed the topic of exceptions to its trumping decision and identified a single exception, the *Bankruptcy and Insolvency Act*... . The *BIA* and the *CCAA* are closely related federal statutes. I cannot conceive that Parliament would specifically identify the *BIA* as an exception, but accidentally fail to consider the *CCAA* as a possible second exception. In my view, the omission of the *CCAA* from s. 222(3) of the *ETA* was almost certainly a considered omission. [para. 43]

119 MacPherson J.A.'s view that the failure to exempt the *CCAA* from the operation of the *ETA* is a reflection of a clear legislative intention, is borne out by how the *CCAA* was subsequently changed after s. 18.3(1) was enacted in 1997. In 2000, when s. 222(3) of the *ETA* came into force, amendments were also introduced to the *CCAA*. Section 18.3(1) was not amended.

120 The failure to amend s. 18.3(1) is notable because its effect was to protect the legislative *status quo*, notwithstanding repeated requests from [page433] various constituencies that s. 18.3(1) be amended to make the priorities in the *CCAA* consistent with those in the *BIA*. In 2002, for example, when Industry Canada conducted a review of the *BIA* and the *CCAA*, the Insolvency Institute of Canada and the Canadian Association of Insolvency and Restructuring Professionals recommended that the priority regime under the *BIA* be extended to the *CCAA* (Joint Task Force on Business Insolvency Law Reform, *Report* (March 15, 2002), Sch. B, proposal 71). The same recommendations were made by the Standing Senate Committee on Banking, Trade and Commerce in its 2003 report, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act*; by the Legislative Review Task Force (Commercial) of the Insolvency Institute of Canada and the Canadian Association of Insolvency and Restructuring Professionals in its 2005 *Report on the Commercial Provisions of Bill C-55*; and in 2007 by the Insolvency Institute of Canada in a submission to the Standing Senate Committee on Banking, Trade and Commerce commenting on reforms then under consideration.

121 Yet the *BIA* remains the only exempted statute under s. 222(3) of the *ETA*. Even after the 2005 decision in *Ottawa Senators* which confirmed that the *ETA* took precedence over the *CCAA*, there was no responsive legislative revision. I see this lack of response as relevant in this case, as it was in *Tele-Mobile Co. v. Ontario*, 2008 SCC 12, [2008] 1 S.C.R. 305, where this Court stated:

> While it cannot be said that legislative silence is necessarily determinative of legislative intention, in this case the silence is Parliament's answer to the consistent urging of Telus and other affected businesses and organizations that there be express language in the legislation to ensure that businesses can be reimbursed for the reasonable costs of complying with evidence-gathering orders. I see the legislative history as reflecting Parliament's intention that

> compensation not be paid for compliance with production orders. [para. 42]

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122 All this leads to a clear inference of a deliberate legislative choice to protect the deemed trust in s. 222(3) from the reach of s. 18.3(1) of the *CCAA*.

123 Nor do I see any "policy" justification for interfering, through interpretation, with this clarity of legislative intention. I can do no better by way of explaining why I think the policy argument cannot succeed in this case, than to repeat the words of Tysoe J.A. who said:

> I do not dispute that there are valid policy reasons for encouraging insolvent companies to attempt to restructure their affairs so that their business can continue with as little disruption to employees and other stakeholders as possible. It is appropriate for the courts to take such policy considerations into account, but only if it is in connection with a matter that has not been considered by Parliament. Here, Parliament must be taken to have weighed policy considerations when it enacted the amendments to the *CCAA* and *ETA* described above. As Mr. Justice MacPherson observed at para. 43 of *Ottawa Senators*, it is inconceivable that Parliament would specifically identify the *BIA* as an exception when enacting the current version of s. 222(3) of the *ETA* without considering the *CCAA* as a possible second exception. I also make the observation that the 1992 set of amendments to the *BIA* enabled proposals to be binding on secured creditors and, while there is more flexibility under the *CCAA*, it is possible for an insolvent company to attempt to restructure under the auspices of the *BIA*. [para. 37]

124 Despite my view that the clarity of the language in s. 222(3) is dispositive, it is also my view that even the application of other principles of interpretation reinforces this conclusion. In their submissions, the parties raised the following as being particularly relevant: the Crown relied on the principle that the statute which is "later in time" prevails; and Century Services based its argument on the principle that the general provision gives way to the specific (*generalia specialibus non derogant*).

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125 The "later in time" principle gives priority to a more recent statute, based on the theory that the legislature is presumed to be aware of the content of existing legislation. If a new enactment is inconsistent with a prior one, therefore, the legislature is presumed to have intended to derogate

from the earlier provisions (Ruth Sullivan, *Sullivan on the Construction of Statutes* (5th ed. 2008), at pp. 346-47; Pierre-André Côté, *The Interpretation of Legislation in Canada* (3rd ed. 2000), at p. 358).

126 The exception to this presumptive displacement of pre-existing inconsistent legislation, is the *generalia specialibus non derogant* principle that "[a] more recent, general provision will not be construed as affecting an earlier, special provision" (Côté, at p. 359). Like a Russian Doll, there is also an exception within this exception, namely, that an earlier, specific provision may in fact be "overruled" by a subsequent general statute if the legislature indicates, through its language, an intention that the general provision prevails (*Doré v. Verdun (City)*, [1997] 2 S.C.R. 862).

127 The primary purpose of these interpretive principles is to assist in the performance of the task of determining the intention of the legislature. This was confirmed by MacPherson J.A. in *Ottawa Senators*, at para. 42:

> ... the overarching rule of statutory interpretation is that statutory provisions should be interpreted to give effect to the intention of the legislature in enacting the law. This primary rule takes precedence over all maxims or canons or aids relating to statutory interpretation, including the maxim that the specific prevails over the general (*generalia specialibus non derogant*). As expressed by Hudson J. in *Canada v. Williams*, [1944] S.C.R. 226, ... at p. 239 ... :
>
> > The maxim *generalia specialibus non derogant* is relied on as a rule which should dispose of the question, but the maxim is not a rule of law but a rule of construction and bows to the intention of the [page436] legislature, if such intention can reasonably be gathered from all of the relevant legislation.

(See also Côté, at p. 358, and Pierre-Andre Côté, with the collaboration of S. Beaulac and M. Devinat, *Interprétation des lois* (4th ed. 2009), at para. 1335.)

128 I accept the Crown's argument that the "later in time" principle is conclusive in this case. Since s. 222(3) of the *ETA* was enacted in 2000 and s. 18.3(1) of the *CCAA* was introduced in 1997, s. 222(3) is, on its face, the later provision. This chronological victory can be displaced, as Century Services argues, if it is shown that the more recent provision, s. 222(3) of the *ETA*, is a general one, in which case the earlier, specific provision, s. 18.3(1), prevails (*generalia specialibus non derogant*). But, as previously explained, the prior specific provision does not take precedence if the subsequent general provision appears to "overrule" it. This, it seems to me, is precisely what s. 222(3) achieves through the use of language stating that it prevails despite any law of Canada, of a province, or "any other law" *other than the BIA*. Section 18.3(1) of the *CCAA* is thereby rendered inoperative for purposes of s. 222(3).

129 It is true that when the *CCAA* was amended in 2005,[2] s. 18.3(1) was re-enacted as s. 37(1) (S.C. 2005, c. 47, s. 131). Deschamps J. suggests that this makes s. 37(1) the new, "later in time" provision. With respect, her observation is refuted by the operation of s. 44(*f*) of the *Interpretation Act*, R.S.C. 1985, c. I-21, which expressly deals with the (non) effect of re-enacting, without significant substantive changes, a repealed provision (see *Attorney General of Canada v. Public Service Staff Relations Board*, [1977] 2 F.C. 663, dealing with the predecessor provision to s. 44(*f*)). It directs that new enactments not be construed as [page437] "new law" unless they differ in substance from the repealed provision:

> **44.** Where an enactment, in this section called the "former enactment", is repealed and another enactment, in this section called the "new enactment", is substituted therefor,
>
> ...
>
> (*f*) except to the extent that the provisions of the new enactment are not in substance the same as those of the former enactment, the new enactment shall not be held to operate as new law, but shall be construed and have effect as a consolidation and as declaratory of the law as contained in the former enactment;

Section 2 of the *Interpretation Act* defines an "enactment" as "an Act or regulation or any portion of an Act or regulation".

130 Section 37(1) of the current *CCAA* is almost identical to s. 18.3(1). These provisions are set out for ease of comparison, with the differences between them underlined:

> **37.** (1) Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

> **18.3** (1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

131 The application of s. 44(*f*) of the *Interpretation Act* simply confirms the government's clearly expressed intent, found in Industry Canada's clause-by-clause review of Bill C-55, where s. 37(1) was identified as "a technical amendment to re-order the provisions of this Act". During second

reading, the Hon. Bill Rompkey, then the Deputy Leader of the Government in the [page438] Senate, confirmed that s. 37(1) represented only a technical change:

> On a technical note relating to the treatment of deemed trusts for taxes, the bill [*sic*] makes no changes to the underlying policy intent, despite the fact that in the case of a restructuring under the CCAA, sections of the act [*sic*] were repealed and substituted with renumbered versions due to the extensive reworking of the CCAA.
>
> (*Debates of the Senate*, vol. 142, 1st Sess., 38th Parl., November 23, 2005, at p. 2147)

132 Had the substance of s. 18.3(1) altered in any material way when it was replaced by s. 37(1), I would share Deschamps J.'s view that it should be considered a new provision. But since s. 18.3(1) and s. 37(1) are the same in substance, the transformation of s. 18.3(1) into s. 37(1) has no effect on the interpretive queue, and s. 222(3) of the *ETA* remains the "later in time" provision (Sullivan, at p. 347).

133 This means that the deemed trust provision in s. 222(3) of the *ETA* takes precedence over s. 18.3(1) during *CCAA* proceedings. The question then is how that priority affects the discretion of a court under s. 11 of the *CCAA*.

134 While s. 11 gives a court discretion to make orders notwithstanding the *BIA* and the *Winding-up Act*, R.S.C. 1985, c. W-11, that discretion is not liberated from the operation of any other federal statute. Any exercise of discretion is therefore circumscribed by whatever limits are imposed by statutes *other* than the *BIA* and the *Winding-up Act*. That includes the *ETA*. The chambers judge in this case was, therefore, required to respect the priority regime set out in s. 222(3) of the *ETA*. Neither s. 18.3(1) nor s. 11 of the *CCAA* gave him the authority to ignore it. He could not, as a result, deny the Crown's request [page439] for payment of the GST funds during the *CCAA* proceedings.

135 Given this conclusion, it is unnecessary to consider whether there was an express trust.

136 I would dismiss the appeal.

* * * * *

APPENDIX

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 (as at December 13, 2007)

11. (1) [Powers of court] Notwithstanding anything in the *Bankruptcy and Insolvency Act* or the *Winding-up Act*, where an application is made under this Act in respect of a company, the court, on

the application of any person interested in the matter, may, subject to this Act, on notice to any other person or without notice as it may see fit, make an order under this section.

...

(3) [Initial application court orders] A court may, on an initial application in respect of a company, make an order on such terms as it may impose, effective for such period as the court deems necessary not exceeding thirty days,

(*a*) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);

(*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(*c*) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

(4) [Other than initial application court orders] A court may, on an application in respect of a company other than an initial application, make an order on such terms as it may impose,

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(*a*) staying, until otherwise ordered by the court, for such period as the court deems necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);

(*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(*c*) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

...

(6) [Burden of proof on application] The court shall not make an order under subsection (3) or

(4) unless

(*a*) the applicant satisfies the court that circumstances exist that make such an order appropriate; and

(*b*) in the case of an order under subsection (4), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

11.4 (1) [Her Majesty affected] An order made under section 11 may provide that

(*a*) Her Majesty in right of Canada may not exercise rights under subsection 224(1.2) of the *Income Tax Act* or any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, in respect of the company if the company is a tax debtor under that subsection or provision, for such period as the court considers appropriate but ending not later than

(i) the expiration of the order,
(ii) the refusal of a proposed compromise by the creditors or the court,
(iii) six months following the court sanction of a compromise or arrangement,

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(iv) the default by the company on any term of a compromise or arrangement, or
(v) the performance of a compromise or arrangement in respect of the company; and

(*b*) Her Majesty in right of a province may not exercise rights under any provision of provincial legislation in respect of the company where the company is a debtor under that legislation and the provision has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest,

penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

for such period as the court considers appropriate but ending not later than the occurrence or time referred to in whichever of subparagraphs (*a*)(i) to (v) may apply.

(2) [When order ceases to be in effect] An order referred to in subsection (1) ceases to be in effect if

(*a*) the company defaults on payment of any amount that becomes due to Her Majesty after the order is made and could be subject to a demand under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, [page442] as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) under any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection; or

(*b*) any other creditor is or becomes entitled to realize a security on any property that could be claimed by Her Majesty in exercising rights under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(A) has been withheld or deducted by a person from a payment to another person [page443] and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection.

(3) [Operation of similar legislation] An order made under section 11, other than an order referred to in subsection (1) of this section, does not affect the operation of

(*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*,

(*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(*c*) any provision of provincial legislation that has a similar purpose to subsection

224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same [page444] effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

18.3 (1) [Deemed trusts] Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

(2) [Exceptions] Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision") nor in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province where

(*a*) that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or

(*b*) the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a "provincial pension plan" as defined in that subsection and the

amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, notwithstanding any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

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18.4 (1) [Status of Crown claims] In relation to a proceeding under this Act, all claims, including secured claims, of Her Majesty in right of Canada or a province or any body under an enactment respecting workers' compensation, in this section and in section 18.5 called a "workers' compensation body", rank as unsecured claims.

...

(3) [Operation of similar legislation] Subsection (1) does not affect the operation of

(*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*,

(*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(*c*) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or
(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as

> defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and [page446] in respect of any related interest, penalties or other amounts.

20. [Act to be applied conjointly with other Acts] The provisions of this Act may be applied together with the provisions of any Act of Parliament or of the legislature of any province, that authorizes or makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them.

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 (as at September 18, 2009)

11. [General power of court] 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.

11.02 (1) [Stays, etc. -- initial application] A court may, on an initial application in respect of a debtor company, make an order on any terms that it may impose, effective for the period that the court considers necessary, which period may not be more than 30 days,

> (*a*) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*;
>
> (*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
>
> (*c*) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

(2) [Stays, etc. -- other than initial application] A court may, on an application in respect of a debtor company other than an initial application, make an order, on any terms that it may impose,

(*a*) staying, until otherwise ordered by the court, for any period that the court considers necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in paragraph (1)(*a*);

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(*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(*c*) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

(3) [Burden of proof on application] The court shall not make the order unless

(a) the applicant satisfies the court that circumstances exist that make the order appropriate; and
(b) in the case of an order under subsection (2), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

...

11.09 (1) [Stay -- Her Majesty] An order made under section 11.02 may provide that

(*a*) Her Majesty in right of Canada may not exercise rights under subsection 224(1.2) of the *Income Tax Act* or any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, in respect of the company if the company is a tax debtor under that subsection or provision, for the period that the court considers appropriate but ending not later than

(i) the expiry of the order,
(ii) the refusal of a proposed compromise by the creditors or the court,
(iii) six months following the court sanction of a compromise or an arrangement,
(iv) the default by the company on any term of a compromise or an

arrangement, or

(v) the performance of a compromise or an arrangement in respect of the company; and

(*b*) Her Majesty in right of a province may not exercise rights under any provision of provincial legislation in respect of the company if the company is a debtor under that legislation and the provision has a purpose similar to subsection 224(1.2) of the *Income [page448] Tax Act*, or refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

for the period that the court considers appropriate but ending not later than the occurrence or time referred to in whichever of subparagraphs (*a*)(i) to (v) that may apply.

(2) [When order ceases to be in effect] The portions of an order made under section 11.02 that affect the exercise of rights of Her Majesty referred to in paragraph (1)(*a*) or (*b*) cease to be in effect if

(*a*) the company defaults on the payment of any amount that becomes due to Her Majesty after the order is made and could be subject to a demand under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) any provision of provincial legislation that has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the [page449] collection of a sum, and of

any related interest, penalties or other amounts, and the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection; or

(*b*) any other creditor is or becomes entitled to realize a security on any property that could be claimed by Her Majesty in exercising rights under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) any provision of provincial legislation that has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection [page450] 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection.

(3) [Operation of similar legislation] An order made under section 11.02, other than the portions of that order that affect the exercise of rights of Her Majesty referred to in paragraph (1)(*a*) or (*b*), does not affect the operation of

(*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*,

(*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(*c*) any provision of provincial legislation that has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

[page451]

37. (1) [Deemed trusts] Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

(2) [Exceptions] Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this

subsection referred to as a "federal provision"), nor does it apply in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province if

> (*a*) that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or
>
> (*b*) the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a "provincial pension plan" as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

Excise Tax Act, R.S.C. 1985, c. E-15 (as at December 13, 2007)

222. (1) [Trust for amounts collected] Subject to subsection (1.1), every person who collects an amount as or on account of tax under Division II is deemed, for all purposes and despite any security interest in the amount, to hold the amount in trust for Her Majesty in right of Canada, separate and apart from the property of the person and from property held by any secured [page452] creditor of the person that, but for a security interest, would be property of the person, until the amount is remitted to the Receiver General or withdrawn under subsection (2).

(1.1) [Amounts collected before bankruptcy] Subsection (1) does not apply, at or after the time a person becomes a bankrupt (within the meaning of the *Bankruptcy and Insolvency Act*), to any amounts that, before that time, were collected or became collectible by the person as or on account of tax under Division II.

...

(3) [Extension of trust] Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the

person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed

> (*a*) to be held, from the time the amount was collected by the person, in trust for Her Majesty, separate and apart from the property of the person, whether or not the property is subject to a security interest, and
>
> (*b*) to form no part of the estate or property of the person from the time the amount was collected, whether or not the property has in fact been kept separate and apart from the estate or property of the person and whether or not the property is subject to a security interest

and is property beneficially owned by Her Majesty in right of Canada despite any security interest in the property or in the proceeds thereof and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 (as at December 13, 2007)

67. (1) [Property of bankrupt] The property of a bankrupt divisible among his creditors shall not comprise

[page453]

> (*a*) property held by the bankrupt in trust for any other person,
>
> (*b*) any property that as against the bankrupt is exempt from execution or seizure under any laws applicable in the province within which the property is situated and within which the bankrupt resides, or
>
> (*b*.1) such goods and services tax credit payments and prescribed payments relating to the essential needs of an individual as are made in prescribed circumstances and are not property referred to in paragraph (*a*) or (*b*),

but it shall comprise

> (*c*) all property wherever situated of the bankrupt at the date of his bankruptcy or that may be acquired by or devolve on him before his discharge, and

(*d*) such powers in or over or in respect of the property as might have been exercised by the bankrupt for his own benefit.

(2) [Deemed trusts] Subject to subsection (3), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a bankrupt shall not be regarded as held in trust for Her Majesty for the purpose of paragraph (1)(*a*) unless it would be so regarded in the absence of that statutory provision.

(3) [Exceptions] Subsection (2) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision") nor in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province where

(*a*) that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or

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(*b*) the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a "provincial pension plan" as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, notwithstanding any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

86. (1) [Status of Crown claims] In relation to a bankruptcy or proposal, all provable claims, including secured claims, of Her Majesty in right of Canada or a province or of any body under an Act respecting workers' compensation, in this section and in section 87 called a "workers' compensation body", rank as unsecured claims.

...

(3) [Exceptions] Subsection (1) does not affect the operation of

(*a*) subsections 224(1.2) and (1.3) of the *Income Tax Act*;

(*b*) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts; or

(*c*) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

[page455]

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

Appeal allowed with costs, ABELLA J. *dissenting.*

Solicitors:

Solicitors for the appellant: Fraser Milner Casgrain, Vancouver.

Solicitor for the respondent: Attorney General of Canada, Vancouver.

1 Section 11 was amended, effective September 18, 2009, and now states:

> **11.** 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.

2 The amendments did not come into force until September 18, 2009.

TAB 3

3 of 4 DOCUMENTS

Case Name:

Crystallex International Corp. (Re)

IN THE MATTER OF the Companies' Creditors Arrangement Act, 1985, c. C-36 as Amended
AND IN THE MATTER OF a Plan of Compromise or Arrangement of Crystallex International Corporation

[2012] O.J. No. 1704

2012 ONSC 2125

91 C.B.R. (5th) 169

2012 CarswellOnt 4577

Court File No. CV-11-9532-00CL

Ontario Superior Court of Justice
Commercial List

F.J.C. Newbould J.

Heard: April 5, 2012.
Judgment: April 16, 2012.

(126 paras.)

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Compromises and arrangements -- Eligible financial contract -- Monitors -- Reports -- Sanction by court -- Motion for approval of DIP financing and Management Incentive Plan, Monitor's reports and extension of stay allowed -- Company's noteholders opposed DIP and MIP -- Company was seeking $3.4 billion in arbitration for Venezuela's unilateral contract termination, more than enough to pay debts -- DIP financing provided $36 million necessary to pursue arbitration -- DIP facility did not prevent plan of arrangement and terms giving financer 35 per cent of arbitration award and corporate control reasonable -- No stay pending appeal as money needed -- MIP independently recommended to retain key employees -- Monitor's reports approved and stay extended.

Bankruptcy and insolvency law -- Proceedings -- Practice and procedure -- Stays -- Pending concurrent proceedings -- Of concurrent proceedings -- Motion for approval of DIP financing and Management Incentive Plan, Monitor's reports and extension of stay allowed -- Company's noteholders opposed DIP and MIP -- Company was seeking $3.4 billion in arbitration for Venezuela's unilateral contract termination, more than enough to pay debts -- DIP financing provided $36 million necessary to pursue arbitration -- DIP facility did not prevent plan of arrangement and terms giving financer 35 per cent of arbitration award and corporate control reasonable -- No stay pending appeal as money needed -- MIP independently recommended to retain key employees -- Monitor's reports approved and stay extended.

Motion for an order approving DIP financing, Management Incentive Plan, Monitor's reports and extending the stay. The company's noteholders objected to the DIP facility and MIP. The company operated a mining project in Venezuela and was unable to pay debts when the Venezuelan government unilaterally terminated its contract, despite all its obligations being met. The company argued its insolvency was due to Venezuela's illegal conduct. The company was seeking $3.4 billion in arbitration, which would be more than enough to pay debts. The DIP facility provided $36 million, provided the financer with 35 per cent of net arbitration proceeds and gave the financer a substantial share in governance. The noteholders objected to the terms and offered their own proposal of a $10 million loan with below-market interest rate and the possibility of another $35 million later. The MIP would set aside 10 per cent of net arbitration proceeds for beneficiaries.

HELD: Motion allowed. The board took legal advice and carefully considered all relevant matters in accepting the DIP financing and terms. There was a robust and competitive bidding process. The company had every intention of negotiating a plan of arrangement, but the DIP facility was not a plan of arrangement and did not require a vote. The rights of the noteholders were not being taken away and it could not be said that giving the financer 35 per cent of net arbitration proceeds would leave insufficient assets to repay outstanding notes or that it was excessive. There was no doubt the company needed at least $36 million to pursue arbitration and required a long term. The noteholders six-month loan and uncertainty about future amounts was not preferable. There was no prospect of the noteholders being paid out prior to arbitration. There was no CCAA prohibition against the board of directors changing and, if the financer's nominees were impairing compromise, the court could remove them. The Monitor supported the bid. The Tenor DIP facility was approved. The noteholders were not granted a stay pending appeal as the financing was needed now, but the order was made subject to undertakings. The MIP was important to retain key personnel during financially difficult times, was independently recommended and not opposed by the Monitor, and so was approved. The Monitor's actions had been commendable and its reports were approved. The stay was extended to July 16, 2012.

Statutes, Regulations and Rules Cited:

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

Companies' Creditors Arrangement Act, 1985. c. C-36, s. 11, s. 11.2(4), s. 11.4(2), s. 11.5(1)

Counsel:

Markus Koehnen, Andrew J.F. Kent and Jeffrey Levine, for Crystallex International Corporation.

Richard B. Swan, S. Richard Orzy and Emrys Davis, for Computershare Trust Company of Canada.

David R. Byers and Maria Konyukhova, for Ernst & Young Inc., Monitor.

Shayne Kukulowicz, for Tenor Special Situations Fund LP.

John T. Porter, for Juan Antonio Reyes.

Robert Frank, for Forbes & Manhattan Inc. and Aberdeen International Inc.

ENDORSEMENT

1 **F.J.C. NEWBOULD J.**:-- Crystallex moves for four orders, the first being an order approving DIP financing pursuant to a credit agreement between Crystallex and Tenor Special Situation I, LLC ("Tenor"), the second being an order extending the stay referred to in paragraph 16 of the Initial Order dated December 23, 2011 until July 16, 2012 or such further date as may be ordered, the third being an order approving a Management Incentive Plan ("MIP") and a Retention Advance Agreement in favour of Robert Fung and the fourth being an order to approve the actions of the Monitor referred to in the second and third reports of the Monitor.

2 The noteholders of Crystallex[1] oppose the Tenor DIP facility. They propose a DIP loan which they would make for a smaller amount and for a shorter term than the Tenor DIP facility. They also oppose the MIP. In order to preserve any appeal rights they may have and may want to assert, they do not consent to an order approving the actions of the Monitor in the second and third reports, but take no position in opposition to the order sought.

3 A shareholder, Mr. J.A. Reyes appeared on the motion to support the Tenor DIP facility and in principle the MIP, but has some concerns regarding the terms of the MIP.

4 Forbes & Manhattan Inc. and Aberdeen International Inc., creditors owed approximately $2.5 million by Crystallex, oppose the Tenor DIP facility and the MIP.

Background to the Financing

5 The history of the business of Crystallex and its mining project in Venezuela has been the

subject of prior decisions in cases brought by the Noteholders. The evidence on the record before me indicates in summary as follows.

6 The principal asset of Crystallex was its right to develop the Las Cristinas gold project in Venezuela. Las Cristinas is one of the largest undeveloped gold deposits in the world containing measured and indicated gold resources of approximately 20.76 million ounces.

7 In September 2002 Crystallex obtained the right to mine the Las Cristinas project through a Mining Operation Contract (the "MOC") with the Corporacion Venezolana de Guayana (the "CVG"), a state-owned Venezuelan corporation. Crystallex complied with all of its obligations under the MOC. Neither the CVG nor the Government of Venezuela raised any material concerns about lack of compliance. The CVG confirmed on several occasions that the MOC was in good standing and that Crystallex was in compliance with it.

8 The Ministry of the Environment advised Crystallex in writing in April 2007 that Crystallex had completed all steps necessary to obtain the required environmental permit. Crystallex was shown a draft of the permit and was told that it would obtain the permit as soon as it had paid certain stamp duties and posted an insurance bond. Crystallex paid the duties, negotiated the bond with the Ministry and posted the bond.

9 On February 3, 2011, despite confirming on several occasions that Crystallex's right to mine the Las Cristinas property continued unchallenged, CVG purported to "unilaterally rescind" the MOC.

10 CVG rationalized its termination of the contract for reasons of "expediency and convenience" and because Crystallex had allegedly "ceased activities for over a year" on the project. Crystallex did not cease activities. It was maintaining the mining site in a shovel-ready state and was awaiting receipt of an environmental permit. Because of Venezuela's refusal to allow Crystallex to exploit Las Cristinas, Crystallex became unable to pay its debts as they became due effective December 23, 2011.

11 Crystallex has a number of liabilities, the most of significant of which is a liability of approximately $100 million in senior unsecured notes that were issued pursuant to a Trust Indenture dated December 23, 2004. The notes were due on December 23, 2011. In addition, Crystallex has other liabilities of approximately CAD$1.2 million and approximately US$8 million.

12 The principal asset of Crystallex is its arbitration claim of US$3.4 billion against Venezuela. In addition, Crystallex has mining equipment with a book value of approximately $10.1 million and cash of approximately $2 million.

13 Crystallex asserts that the insolvency in which it finds itself is not attributable to poor business judgment by Crystallex but to the illegal conduct of the Venezuelan government in refusing to let Crystallex develop Las Cristina, even though Crystallex had the undisputed contractual right to do so.

Arbitration proceedings

14 On February 16, 2011 Crystallex filed a Request for Arbitration with the International Centre for the Settlement of Investment Disputes ("ICSID") against Venezuela pursuant to a Bilateral Investment Treaty between Canada and Venezuela. ICSID is a mechanism through which private investors can seek legal redress against a foreign government for conduct that might be otherwise immune from suit. In the arbitration, Crystallex seeks compensation of $3.4 billion plus interest as full compensation for the loss of its investment.

15 The Arbitration Tribunal held its first procedural meeting on December 1, 2011 in Washington, DC. At that hearing, the Tribunal established Washington, DC as the seat of the arbitration proceeding, and established a timetable for the arbitration. Pursuant to the timetable, Crystallex delivered its written case on February 10, 2012. Crystallex's written case comprises fourteen volumes of detailed witness statements, expert's reports, exhibits, law and argument. Its memorial summarizing the evidence, law and argument extends to 226 pages. Venezuela is required to respond to Crystallex's case by August 31, 2012. The hearing of the arbitration is scheduled for two weeks beginning on November 11, 2013.

16 The valuation evidence Crystallex submitted with its ICSID case claims damages of $3.4 billion plus interest. While the result of the arbitration is unknown, if it is successful, and the award is collected, there will be far more available than necessary to pay the outstanding debts of Crystallex. It is also clear that any meaningful recovery for the creditors and possibly shareholders will require some success in the arbitration, either by a collectible award or a settlement.

DIP financing selection process

17 In accordance with paragraph 12 of the Initial Order, Crystallex, with the assistance of its counsel and its financial advisor, commenced a process to seek DIP financing of $35 million with a term of December 13, 2014.

18 With the approval of the Monitor, Crystallex hired a financial advisor, Skatoff & Company, LLC based in New York City. Mr. Skatoff is an independent financial advisory firm focused on debt advisory services, financial restructuring advisory services, financing advisory services and M&A services.

19 Crystallex, in consultation with Mr. Skatoff and on its recommendation, prepared a set of bid procedures to govern the solicitation of bids to provide DIP financing to Crystallex. The bid procedures were approved by the Monitor. The bid procedures are referred to in some detail in my endorsement of January 25, 2012. They included a provision whereby the DIP lender could obtain a "back-end entitlement" of up to 49% of the arbitration proceeds.

20 The bid procedures provided that Crystallex would only consider bids from qualified bidders. A qualified bidder was one who, among other things, complied with certain participation

requirements including the submission of a participation package.

21 As a result of the DIP financing auction, a small number of qualified bidders ultimately submitted proposals for the DIP financing. Among the bidders were the three hedge funds that hold approximately 77% of Crystallex's senior unsecured notes.

22 Ultimately Mr. Skatoff recommended, and the board of Crystallex agreed, to accept the terms of the Tenor DIP financing now before the court for approval.

Proposed Tenor DIP financing

23 The Tenor DIP facility contains the following material financial terms:

(a) Tenor will advance $36 million to Crystallex due and payable on December 31, 2016. This period for the loan is based on Crystallex's arbitration counsel's assessment of the likely timing of a decision from the arbitral tribunal and collection of the award.

(b) The advances will be in four tranches, being $9 million upon execution of the loan documentation and approval of the facility by court order in Ontario, the second being $12 million upon any appeal of the Ontario court order approving the facility being dismissed and upon a U.S court order approving the facility, the third being $10 million when Crystallex has less than $2.5 million in cash and the fourth being $5 million when Crystallex again has less than $2.5 million in cash.

(c) The loans are to be used to (i) repay an interim bridge loan of $3.25 million advanced by Tenor with court approval of January 20, 2012 and payable on April 16, 2012, (ii) fees and expenses in connection with the facility, (iii) general corporate expenses of Crystallex including expenses of the restructuring proceedings and of the arbitration in accordance with cash flow statements and budgets of Crystallex approved by Tenor from time to time.

(d) Crystallex will pay Tenor a $1 million commitment fee.

(e) $35 million of the loan amount will bear PIK interest (payment in kind, meaning it is capitalized and payable only upon maturity of the loan or upon receipt of the proceeds of the arbitration) at the rate of 10% per annum compounded semi-annually.

(f) Tenor will receive additional compensation equal to 35% of the net proceeds of any arbitral award or settlement, conditional upon the second tranche of the loan being advanced. Net proceeds of the award or settlement is defined as the amount remaining after payment of principal and interest on the DIP loan, taxes and proven and allowed unsecured claims against Crystallex, including the noteholders, the latter of which

will have a special charge for the unsecured amounts owing. Alternatively, Tenor can convert the right to additional compensation to 35% of the common shares of Crystallex. This conversion right is apparently driven by tax considerations.

24 The Tenor DIP facility also provides for the governance of Crystallex to be changed to give Tenor a substantial say in the governance of Crystallex. More particularly:

(a) Crystallex shall have a reduced five person board of directors, being two current Crystallex directors, two nominees of Tenor and an independent director selected by agreement of Crystallex and Tenor.

(b) The independent director shall be chair of the board of directors and shall not have a second-casting or tie-breaking vote.

(c) The independent director shall be appointed a special managing director and shall have all the powers of the board of directors to (i) the conduct of the reorganization proceedings in Canada and in the U.S. and the efforts of Crystallex to reorganize the pre-filing claims of the unsecured creditors, (ii) any matters relating to the rights of Crystallex and Tenor as against the other under the facility, (iii) the administration of the MIP to the extent not otherwise delegated to the bonus pool committee under the MIP, and (iv) to retain any advisor in respect of these matters. The special manager shall first consult with a non-board advisory panel, consisting of the three Crystallex directors who will step down from the board, and consider in good faith their recommendations.

(d) With respect to matters that may not at law be delegable to the special managing director, he will be required to obtain board approval. If the Tenor nominees use their votes to block that approval, Tenor will forfeit its 35% additional compensation.

25 The Tenor DIP facility contains proscribed rights of Tenor in the event of default. Tenor may seize and sell assets other than the arbitration proceeding (i.e. any cash and unsold mining equipment). It may not sell the arbitration claim. If there is a default before any arbitration award, Tenor would have the right to apply to court to have the Monitor or a Canadian receiver and manager appointed to take control of the arbitration proceedings. If such application were not granted, Tenor would be entitled to exercise the rights and remedies of a secured creditor pursuant to an order, the loan documentation or otherwise at law.

Proposed Noteholders DIP Loan and Plan

26 The noteholders propose a DIP loan of $10 million with a simple interest rate of 1% repayable on October 15, 2012. This was essentially the same as the interim bridge loan of $10 million with simple interest of 1% proposed by the noteholders that would have been repaid on April 16, 2012

that was not accepted by Crystallex. It is quite clear that the interest rate is far below market in the circumstances of Crystallex, and it is referred to in the noteholders factum as "exceptionally favourable".

27 During the process to find a DIP lender satisfactory to Crystallex and its advisors, the noteholders were asked to increase their proposed loan to $35 million but they refused. However, in his affidavit Mr. Mattoni on behalf of the noteholders stated that the noteholders would in the future be prepared under certain circumstances, if required by the court, to advance a DIP loan on the same terms as the Tenor DIP facility. He stated that the noteholders would do so in the event that prior to October 1, 2012, the court orders that such long-term financing is appropriate and necessary. The noteholders would reserve their ability as creditors to continue to oppose the need for such a loan and any stay extensions or attempts to secure such long-term financing outside of a plan of compromise. The $10 million which they provided in interim financing would be repaid from this financing such that the net effect of the financing would be the same as that of the Tenor DIP facility. During argument on this motion, Mr. Swan said that the noteholders were not prepared to agree to such a $35 million facility at this time but only at some future time as the $10 million facility they now proposed became due.

28 The noteholders have also now proposed a restructuring plan, said to be in response to the Tenor DIP and the MIP. This was first proposed by Mr. Mattoni in his affidavit of March 27, 2012 as a proposal of the noteholders. At that time, he did not have any internal authority from the QVT fund of which he is the investment manager, or from any of the other noteholders, to make such proposal. This was shored up as indicated in his further affidavit of April 4, 2012 served just before the hearing of this motion. The noteholders do not ask for approval of this plan on this motion, but put it forward as indicating a good faith intention to bargain for a plan. The noteholders plan would:

a) provide $10 million at 1% interest in a single-draw to meet Crystallex's funding needs over the next several months while a plan is negotiated;
b) provide $35 million to the Company in a straight exchange for 22?9% of Crystallex's equity;
c) exchange all outstanding debt for equity;
d) secure approximately 14% of the remaining equity for existing shareholders; and
e) provide incentives to management at a lesser level than the MIP. It would be up to the post-emergence board to ensure that management is properly incentivized, which could involve other compensation as well.

Management Incentive Plan

29 In addition to approval of the DIP, Crystallex seeks approval of a Management Incentive Plan ("MIP") for certain of its key employees. The fundamental terms of the MIP are as follows:

(a) An amount equal to up to 10% of the first $700 million in net proceeds of

the arbitration award and an amount equal to up to 2% of the net proceeds in excess of $700 million will be reserved as a retention pool for key management employees.

(b) The amount to be retained in this pool is the amount remaining after payment of the outstanding principal and interest on the DIP loan, outstanding operating and professional expenses, the unpaid claims of noteholders and other stayed unsecured creditors, together with post-filing interest and all taxes payable by the company on the award.

(c) The size of the pool shall not exceed 10% of the net proceeds of the arbitral award or one quarter of the amount that is available to shareholders of Crystallex after satisfaction of any additional compensation owing to Tenor under the loan agreement.

(d) A compensation committee consisting of three persons who are currently independent directors of Crystallex and who are expected to retire from the board in accordance with the governance provisions of the Tenor DIP facility, will determine the retention payment paid to each beneficiary of the MIP. The compensation committee will be entitled to distribute as much or as little of the retention pool as they see fit. Amounts remaining unpaid from the retention pool will be returned to Crystallex.

30 Crystallex also proposes that there be a MIP charge to secure the payments, the charge to be subordinate to the Administration Charge, the DIP Charge, the Directors' Charge and the Pre-filing Unsecured Creditors Charge.

31 Also sought for approval is a retention agreement for Mr. Fung which provides that at the end of each calendar quarter during 2012 and 2013 the board of Crystallex will pay a retention advance of $125,000 per quarter to Mr. Fung. The making of each payment will be at the discretion of the board but only to the extent that he remains properly engaged in the arbitration. Those payments are to be treated as if they were pre-payments of any payments that would otherwise be awarded to Mr. Fung from the retention pool under the MIP and therefore reduce any such amount he may receive from the retention pool.

DIP loan approval analysis

32 Section 11.2 of the CCAA provides that a court may provide security in favour of an interim or DIP lender who agrees to lend to the debtor company having regard to its cash-flow statement. Section 11.2 (4) provides:

> (4) In deciding whether to make an order, the court is to consider, among other things,
>
> (*a*) the period during which the company is expected to be subject to

> proceedings under this Act;
>
> (*b*) how the company's business and financial affairs are to be managed during the proceedings;
>
> (*c*) whether the company's management has the confidence of its major creditors;
>
> (*d*) whether the loan would enhance the prospects of a viable compromise or arrangement being made in respect of the company;
>
> (*e*) the nature and value of the company's property;
>
> (*f*) whether any creditor would be materially prejudiced as a result of the security or charge; and
>
> (*g*) the monitor's report referred to in paragraph 23(1)(*b*), if any.

33 Crystallex relies on the business judgment rule to support the decision of its board of directors to accept the Tenor DIP facility. It is clear that the business judgment rule can apply to a debtor in CCAA proceedings. In *Re Stelco*, (2009), 9 C.B.R. (5th) 135 (Ont. C.A.), Blair J.A. stated in that CCAA proceeding:

> 65. ... It is well-established that judges supervising restructuring proceedings - and courts in general - will be very hesitant to second-guess the business decisions of directors and management. As the Supreme Court of Canada said in *Peoples, [2004] 3 S.C.R. 461, supra*, at para. 67:
>
> > Courts are ill-suited and should be reluctant to second-guess the application of business expertise to the considerations that are involved in corporate decision making ...

34 The noteholders point to *Kerr v. Danier Leather Inc*, [2007] 3 S.C.R. 331 per Binnie J. at para. 54 in which he stated that the business judgment rule could not be used to qualify or undermine the duty of disclosure required by the *Securities Act* and *Bennett v. Bennett Environmental Inc.* 2009 ONCA 198 per Lang. J.A. in which she held that whether a director could be indemnified depended

on the application of section 123(4) of the CBCA and not the business judgment rule.

35 I accept that in considering whether security under a DIP loan should be ordered, a court cannot ignore the factors directed to be considered in section 11.2 (4) of the CCAA and could not order such security if a consideration of those factors led to an opposite conclusion. But in my view those factors are not the only factors that can be considered, as section 11.2(4) directs a court to consider the listed factors "among other things". One of the considerations that in my view can be taken into account is the exercise or lack thereof of business judgment by the board of directors of a debtor corporation in considering DIP financing.

(i) Consideration of the Tenor DIP facility

36 In this case, the Crystallex board took legal advice from its solicitors McMillan LLP and financial advice from Mr. Skatoff. I am satisfied that they carefully considered the relevant matters leading to the decision to accept the terms of the Tenor DIP financing, including giving consideration to the noteholders' proposed DIP financing of $10 million to October, 2012, and that they acted on an informed basis and in good faith with a view to the best interests of Crystallex and its stakeholders. See the affidavits of Mr. Fung at paras. 52 to 67 and the reply affidavit of Mr. van't Hof at paras. 9 to 12. That being said, I must consider the contentions of the parties and the factors as set out in section 11.2 (4).

37 The noteholders have made a number of objections to the Tenor DIP financing.

38 They contend that Crystallex should have sought sufficient financing to pay the noteholders in full, as was attempted prior to the CCAA filing. The evidence indicates, however, that Mr. Skatoff attempted to do so with the market but the message he received back consistently was that the market had no interest in paying out existing noteholders at 100 cents on the dollar in a context where the notes were trading at a significant discount to par. Mr. Mattoni himself said on cross-examination that he did not believe it would be possible to raise sufficient money on the market to pay out the noteholders, as did the noteholder's financial expert witness Mr. Glenn Sauntry.

39 Mr. Mattoni in his affidavit states that the Tenor DIP facility was a pre-ordained coronation rather than the result of a competitive bidding process. There is no evidentiary basis for this suggestion. It is clear from the evidence of Mr. Skatoff, Mr. Fung and Mr. van't Hof and from the Monitor's report that there was a robust competitive bidding process and that full consideration right up to the last minute was given to other bidders. The Monitor stated it its report that from its observation of the process, it saw no evidence that Tenor was afforded preferential treatment over other participants in the process. It is also clear that the noteholders' $10 million bid was considered by the board of Crystallex and, based on advice from its advisors, not accepted. Thus any complaint from the noteholders on this score could only be that the Tenor bid was higher than market pricing for the facility. They had no such evidence and on cross-examination their financial expert Mr. Sauntry acknowledged that he could not say that the Tenor bid was not reflective of market pricing.

40 The noteholders also complain that Mr. Skatoff did not undertake a valuation of Crystallex. The response of Crystallex is that it was not Mr. Skatoff's job to do that. In light of the fact that the main asset of Crystallex is the arbitration claim, Mr. Skatoff in my view would be in a poor position to value Crystallex.

41 Mr. Sauntry in his report attempted to value the arbitration claim in different ways. He is not a lawyer and has no knowledge of the treaties involved or of the merits of the arbitration claim. He made assumptions in his cash flow analysis that, based on the reply expert report of Mr. Dellepiane, which I have no reason to doubt as he was intimately involved in the preparation of the arbitration claim, indicate Mr. Sauntry's lack of knowledge of the basis of the claim. Regarding Mr. Sauntry's analysis in (i) implying a value to the arbitration claim from an analysis of the Tenor DIP proposal and stating that in substance that proposal is a sale of a percentage of Crystallex's assets to Tenor and (ii) using the market value of Crystallex's securities as a proxy for enterprise value, I accept the reply affidavit of Mr. Skatoff, and in particular paragraphs 34 to 41, as reason to doubt Mr. Sauntry's analysis. As well, Mr. Sauntry's evidence on cross-examination, and in particular that referred to in paragraphs 8 to 12 of the Summary of Key Points From Cross-examinations, indicates little reliability should be placed on Mr. Sauntry's evidence.

42 In any event, in light of the lack of evidence from the noteholders that the Tenor bid was not above market, the contention that Mr. Skatoff did not undertake a valuation of Crystallex or of the arbitration claim is of little moment.

43 The noteholders also contend that whereas the bid process spelled out terms that must not be contained in a bid and provided that some terms were to be discouraged, the Tenor bid in the end contained some such terms. In those circumstances, the noteholders contend that Crystallex should have re-canvassed the market. Mr. Skatoff's evidence is that other bidders presented loan terms that would have resulted in similarly extensive changes to the loan document that accompanied the bid packages. The world of restructuring is not a perfect world. A company seeking DIP financing can tell the market what it wants, but cannot dictate its terms if the market tells it otherwise. The alternative is to walk away from the market. Regarding the changes sought by the market, the Monitor in its report states:

> 50. During the negotiations, all bidders requested amendments to the template version of the loan agreement posted on the Monitor's website as part of the CCAA Financing Procedures. The Monitor is of the view that such requests are typical in any bidding or investment raising process. The Monitor observed that all parties were provided with the template loan agreement and, as is common in processes such as the CCAA Financing Procedures, the final forms of the selected commitment letter and senior credit agreement deviate from the template agreement.

44 The noteholders take a fundamental objection to the Tenor DIP facility on the basis that it is

inconsistent with the purposes of the CCAA and case law dealing with DIP loans. The noteholders say that it is not interim financing but a forced restructuring plan prejudicial to them and that it should not proceed without a vote as required by the CCAA for a plan of arrangement or compromise.

45 *Cliffs Over Maple Bay Investments Ltd. v. Fisgard Capital Corp*., (2008) 46 C.B.R. (5th) 7 (B.C.C.A.) is authority for the proposition that a stay under the CCAA should not be continued if the debtor company does not intend to propose a compromise or arrangement to its creditors, and DIP financing should not be authorized to permit the debtor company to pursue a restructuring plan that does not involve an arrangement or compromise with its creditors. In that case, the debtor wanted to obtain financing to complete the construction of a golf course development without proposing an arrangement or compromise with its creditors.

46 The noteholders seize upon a statement made by Mr. Fung in his affidavit filed on the initial application leading to the Initial Order in which he said:

> Crystallex strongly desires to pursue the arbitration and have stayed all claims against it until the arbitration has been settled or Crystallex has realized on an arbitration award, at which point Crystallex expects that all creditors would be paid in full to the extent of their proven claims.

47 While there is no doubt that Mr. Fung made that statement, I think it needs to be considered in light of the reality agreed by the parties that the only way any of the creditors will receive any substantial cash payment is from the proceeds of the arbitration. This would be the case whether a plan of arrangement could be agreed or not. Also Mr. Mattoni agreed on cross-examination that Crystallex's goal of pursuing the arbitration and using the proceeds to pay creditors in full did not prevent Crystallex from giving creditors some additional benefit in a plan of arrangement.

48 Moreover, often statements are made in CCAA proceedings about the intention of a party that later change. Mr. Koehnen made clear in argument that Crystallex has every intention to attempt to negotiate a plan of arrangement with the noteholders and that this has already been going on now on a without prejudice basis. He said the purpose of the stay to July 16, 2012 is to negotiate a compromise with the noteholders during that time period. I accept that statement. The situation is not the same as in *Cliffs Over Maple Bay*.

49 Is the Tenor DIP facility a plan of arrangement or compromise requiring a vote? In my view it is not.

50 A "plan of arrangement" or a "compromise" is not defined in the CCAA. It is, however, to be an arrangement or compromise between a debtor and its creditors. The Tenor DIP facility is not on its face such an arrangement or compromise between Crystallex and its creditors. Importantly the rights of the noteholders are not taken away from them by the Tenor DIP facility. The noteholders are unsecured creditors. Their rights are to sue to judgment and enforce the judgment. If not paid,

they have a right to apply for a bankruptcy order under the BIA. Under the CCAA, they have the right to vote on a plan of arrangement or compromise. None of these rights are taken away by the Tenor DIP.

51 I note that in this case the practical exercise of the rights of the noteholders is very problematical because of issues raised in Mr. Fung's confidential affidavit no. 2.

52 The noteholders contend that giving Tenor 35% of the arbitration proceedings will take away from Crystallex a substantial amount of equity making a compromise more difficult and less available for the unsecured creditors.

53 In *Re Calpine Canada Energy Inc*. (2007) 35 C.B.R. (5th) 1 (Alta. Q.B.), leave to appeal denied (2007) 35 C.B.R. (5th) 27, it was contended that a settlement of several claims in a complex cross-border restructuring constituted a plan of arrangement or compromise and thus required a vote under the CCAA by the creditors affected. It was contended that the settlement left less assets available for the Canadian unsecured creditors. In rejecting this contention, Romaine J. stated the following:

> 12. The primary objection is that the GSA [global settlement agreement] amounts to a plan of arrangement and, therefore, requires a vote by the Canadian creditors. The Opposing Creditors support their submissions by isolating particular elements of the GSA and characterizing them as either a compromise of their rights or claims or as examples of imprudent concessions made by the CCAA Debtors in the negotiation of the GSA. These specific objections will be analyzed in the next part of these reasons, but, taken together, they fail to establish that the GSA is a compromise of the rights of the Opposing Creditors for two major reasons:
>
> (b) the Opposing Creditors blur the distinction between compromises validly reached among the parties to the GSA and the effect of those compromises on creditors who are not parties to the GSA. ... If rights to a judicial determination of an outstanding issue have not been terminated by the GSA, which instead provides a mechanism for their efficient and timely resolution, those rights are not compromised.
>
> 19 ... While settlements made in the course of insolvency proceedings may, in practical terms, result in a diminution of the pool of assets remaining for division, this is not equivalent to a compromise of substantive rights.
>
> 51. The GSA is not linked to or subject to a plan of arrangement. I have found that it

> does not compromise the rights of creditors that are not parties to it or have not consented to it, and it certainly does not have the effect of unilaterally depriving creditors of contractual rights without their participation in the GSA.
>
> 55. I am satisfied that the GSA is not a plan of compromise or arrangement with creditors. Under its terms, as agreed among the CCAA Debtors, the U.S. Debtors and the ULC1 Trustee, certain claims of those participating parties are compromised and settled by agreement. Claims of creditors who are not parties to the GSA either will be paid in full (and thus not compromised) as a result of the operation of the GSA, or will continue as claims against the same CCAA Debtor entity as had been claimed previously.

54 In refusing leave to appeal from the decision of Romaine J., O'Brien J.A. stated:

> 34. ... The GSA does not change its status as a creditor of those companies, nor does it bar the applicant from any existing claims against those companies.
>
> 35. ... the fact that the GSA impacts upon the assets of the debtor companies, against which the applicant may ultimately have a claim for any shortfall experienced by it, is a common feature of any settlement agreement and as earlier explained, does not automatically result in a vote by the creditors. The further fact that one of the affected assets of the debtor companies is a cause of action, or perhaps, more correctly, a possible cause of action, does not abrogate the rights of a creditor albeit there may be less monies to be realized at the end of the day.

55 While this case is not binding on me, it is persuasive and makes sense. It is also consistent with authorities in Ontario that a sale of assets or a settlement in a CCAA before a plan of compromise is put forward may be authorized even if there will be insufficient assets to retire the creditor claims in full. See *Re Canadian Red Cross Society* (1998), 5 C.B.R. (4th) 299.

56 In this case, it cannot be said that there will be insufficient assets coming from the arbitration to repay all of the outstanding notes in full, which at present is approximately $115 million. Even the valuation of Mr. Sauntry, which I do not accept as reliable, indicates far more than that as a possible outcome of the arbitration. While the outcome of the claim cannot be known at this stage, it is a claim for $3.4 billion dollars in circumstances in which Crystallex spent approximately $500 million on the development of the mine.

57 The fundamental purpose of the CCAA is well established, and indicates that flexibility is required in dealing with any particular case. In *A.G. Can. v. A.G. Que. (sub. nom. Reference re Companies' Creditors Arrangement Act)*, [1934] S.C.R. 659, the following was stated:

> ... the aim of the Act is to deal with the existing condition of insolvency in itself to enable arrangements to be made in view of the insolvent condition of the company under judicial authority which, otherwise, might not be valid prior to the initiation of proceedings in bankruptcy. *Ex facie* it would appear that such a

> scheme in principle does not radically depart from the normal character of bankruptcy legislation."
>
> The legislation is intended to have wide scope and allow a judge to make orders which will effectively maintain the status quo for a period while the insolvent company attempts to gain the approval of its creditors for a proposed arrangement which will enable the company to remain in operation for what is, hopefully, the future benefit of both the company and its creditors.

58 Since 1934, of course, there has been wide experience in dealing with the CCAA, and it has been an evolving experience. In *Re Canadian Red Cross,* Blair J. (as he then was) approved the sale of the assets of the debtor that would result in the estate having less than sufficient money to pay all of its creditors in full, and before a plan of compromise was put forward. He discussed the flexibility involved in these terms:

> 45. It is very common in CCAA restructurings for the Court to approve the sale and disposition of assets during the process and before the Plan if formally tendered and voted upon. ... The CCAA is designed to be a flexible instrument, and it is that very flexibility which gives it its efficacy. As Farley J. said in *Dylex, [1995] O.J. No. 595, supra* (p. 111), "the history of CCAA law has been an evolution of judicial interpretation". It is not infrequently that judges are told, by those opposing a particular initiative at a particular time, that if they make a particular order that is requested it will be the first time in Canadian jurisprudence (sometimes in global jurisprudence, depending upon the level of the rhetoric) that such an order has made! Nonetheless, the orders are made, if the circumstances are appropriate and the orders can be made within the framework and in the spirit of the CCAA legislation. Mr. Justice Farley has well summarized this approach in the following passage from his decision in *Re Lehndorff General Partner* (1993), 17 C.B.R. (3d) 24, at p. 31, which I adopt:
>
> > The CCAA is intended to facilitate compromises and arrangements between companies and their creditors as an alternative to bankruptcy and, as such, is remedial legislation entitled to a liberal interpretation. It seems to me that the purpose of the statute is to enable insolvent companies to carry on business in the ordinary course or otherwise deal with their assets so as to enable plan of compromise or arrangement to be prepared, filed and considered by their creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors. See the preamble to and sections 4, 5, 7, 8 and 11 of the CCAA (a lengthy list of authorities cited here is omitted).

> The CCAA is intended to provide a structured environment for the negotiation of compromises between a debtor company and its creditors for the benefit of both. Where a debtor company realistically plans to continue operating or to otherwise deal with its assets but it requires the protection of the court in order to do so and it is otherwise too early for the court to determine whether the debtor company will succeed, relief should be granted under the CCAA (citations omitted)

59 In that case, Blair J. considered the factors in *Soundair* in deciding whether to approve of the sale, being whether the receiver has made a sufficient effort to get the best price and has not acted improvidently; to consider the interests of the parties, to consider the efficacy and integrity of the process by which offers are obtained and to consider whether there has been unfairness in the working out of the process. Those factors are consistent with the factors to be taken into account in considering whether security for a DIP loan should be approved, and as the Tenor DIP facility involves a grant of a financial interest in part of the assets of Crystallex, being a percentage of the arbitration award, it seems to me that they can be looked at in this case.

60 It was contended by the noteholders that the size of a loan of $36 million, an amount calculated to complete and collect the arbitration, was not in accordance with the purposes of a DIP loan as it would take Crystallex beyond what is required before any reorganization. However this complaint regarding the size of the loan was not strenuously pursued in argument, no doubt because of the new position of the noteholders that it would fund that amount on the terms of the Tenor DIP loan if later required and because of the provision in the proposed plan of arrangement put forward by the noteholders that it would provide $36 million in funding in return for an equity stake in Crystallex. There seems no doubt that the parties agree that at least $36 million is required to pursue the arbitration.

61 The noteholders also contend that the term of the loan by Tenor is far too long and that it indicates an attempt by Crystallex to do an end run around the need to propose a plan of arrangement as the term would extend beyond the date of an anticipated award. I have already dealt with the issue of Crystallex proposing a plan of arrangement. The noteholders contend that the DIP loan, at least initially, should not extend beyond October, 2012 as by then a plan should have been negotiated. However, both sides agree that the only way that any substantial cash will be available to Crystallex or its creditors will be from the arbitration and that it will be necessary to prosecute the arbitration long after October, 2012. The proposed plan of the noteholders recognizes this as it proposes a $36 million injection for the purposes of prosecuting the arbitration. The $36 million figure is based on a projection of expenditures going far beyond 2012. That is, both sides agree that it will be necessary to have financing for the arbitration that will continue after October, 2012. The term of the Tenor DIP loan as to when the loan becomes due in itself is not an impediment to a restructuring.

62 In my view, the term of the loan is not the substantive issue, so long as Crystallex intends to negotiate if possible an acceptable plan of arrangement or compromise, which it has indicated it intends to do. One of the factors required to be considered under section 11.2(4) is the time during which Crystallex is expected to be subject to the CCAA proceedings. Like many cases, it is not clear when these proceedings may be over. However, as the $36 million financing is going to be required whether Crystallex is out from under the CCAA in a short or longer period, and as the expenditures are to last for a few years, this factor of the time during which Crystallex is expected to be subject to the CCAA proceeding is not a determinative factor.

63 The noteholders also contend that Tenor has been given control over Crystallex and the restructuring process by reason of the changes in the corporate governance required by the Tenor DIP facility. There is no doubt that Tenor has been given substantial governance rights, including the right to name two of the five directors and the right to agree on who the independent director shall be. An issue is whether the governance provisions are too intrusive for a DIP loan, which according to case law relied on by the noteholders should not be excessive or inappropriate. I note that there is no prohibition in the CCAA against the board of directors changing at the hands of the debtor. There is a provision allowing the court to remove directors, which I shall later discuss.

64 Any DIP lender wants to obtain as much control as possible over the affairs of the debtor during the term of the DIP financing, and terms are often imposed to that end. In this case, given the extreme hostility of the noteholders to the board and management of Crystallex over its actions over the few years prior to the arbitration being commenced, it is not surprising that Tenor has demanded what it has. The fact that Tenor at the last minute changed the governance terms that it was prepared to live with, and that the Crystallex board was not happy with the change, does not in itself mean that those terms should not be approved.

65 To put up the financing and have it subject to change by the noteholders or Crystallex would make no economic sense to Tenor or to any other DIP lender in the circumstances of this case. Like the noteholders and shareholders, Tenor will only be able to have its loan repaid from the proceeds of the arbitration, and it has bargained for what it perceives to be necessary protection for that. I agree with the noteholders that the CCAA is not about protecting new DIP lenders. However, the issue is whether the protections negotiated in order to obtain the DIP loan from Tenor are reasonable or excessive.

66 Even if there were a prospect of money being raised by Crystallex in some fashion to pay out the noteholders prior to an arbitration award or settlement, which on the evidence I have referred to is not the case, including the issues referred to in Mr. Fung's confidential affidavit no. 2, and the opinion of Freshfields, as a practical matter this is not a case in which the noteholders have any realistic steps to try to cash out now before the arbitration claim is dealt with.[2] A restructuring under the CCAA, or any bankruptcy of Crystallex, is not going to change that. The market cap of Crystallex is far too small to repay the noteholders, even if they were given 100% of the equity of Crystallex.

67 The terms of the Tenor Dip facility give Tenor no right to conduct the reorganization proceedings in Canada and in the U.S. or interfere with the efforts of Crystallex to reorganize the pre-filing claims of the unsecured creditors. That will be in the hands of the independent/special managing director who will be required to consult with the non-board advisory panel consisting of the three directors of Crystallex who will step down from the board. With respect to matters that may not at law be delegable to the special managing director, he will be required to obtain board approval and if the Tenor nominees use their votes to block that approval, Tenor will forfeit its 35% additional compensation. Tenor is obviously not going to want to put itself in that position.

68 Tenor recognizes that it cannot conduct the arbitration proceeding. Under the terms of the Tenor DIP facility, if there is a default before any arbitration award, Tenor would have the right to apply to court to have the Monitor or a Canadian receiver and manager appointed to take control of the arbitration proceedings. Whether it would make such an application is a question mark, and likely would depend on whether Crystallex were put into bankruptcy. There would likely be no other reason for wanting someone other than the Crystallex board to have control over the conduct of the arbitration.

69 As a practical matter, the conduct of the arbitration will no doubt be in the hands of Freshfields who have the knowledge and expertise. Mr. Mattoni in his affidavit filed on behalf of the noteholders agreed that the arbitration is really in the hands of litigation counsel. As well, the management personnel of Crystallex that have been involved in the claim in presenting evidence and instructing counsel regarding the evidentiary issues are going to have to continue to be involved in order to prosecute the claim. Their failure to do so would compromise the claim.

70 If any director, whether nominees of Crystallex or of Tenor, is unreasonably impairing the possibility of a viable compromise, the court under s. 11.5(1) of the CCAA has the power to remove such director. That section provides:

> 11.5(1) The court may, on the application of any person interested in the matter, make an order removing from office any director of a debtor company in respect of which an order has been made under this Act if the court is satisfied that the director is unreasonably impairing or is likely to unreasonably impair the possibility of a viable compromise or arrangement being made in respect of the company or is acting or is likely to act inappropriately as a director in the circumstances.

71 The noteholders point out that section 8.1(t) of the DIP facility makes it an event of default of the DIP loan if a Tenor nominee director is removed from the board without the consent of Tenor except "by reason of misconduct" of the director, and assert that "misconduct" is a considerably different standard from "unreasonably impairing" in section 11.5(1) of the CCAA, thus restricting a court's ability to remove a director for unreasonably impairing a compromise or arrangement. Of course, any application under the section would turn on the particular facts, but it would certainly be

arguable that if a director were unreasonably impairing a compromise or arrangement, that could constitute misconduct, particularly as the purpose of a CCAA proceeding is to encourage a consensual compromise or arrangement.

72 One of the factors required to be considered under section 11.2(4) is whether Crystallex's management has the confidence of its major creditors. There is no doubt from the prior litigation that the noteholders expressed extreme displeasure at the steps taken by its board and management to try to come to some accommodation with Venezuela to maintain the rights to the Las Cristinas mine project. The noteholders maintained that Crystallex should stop spending money and commence the arbitration. That of course is now water under the bridge and the only business of Crystallex is the arbitration that has been commenced. The noteholders did not previously take the position that the management should not be involved in the arbitration, nor do they now raise any such objection. The Monitor notes in its report that the noteholders' proposed plan contemplates keeping existing management. It is clear that the management who have been involved in the arbitration are going to be needed further, and this is not a situation in which the noteholders could want to insert themselves instead of management in the conduct of the arbitration. As Mr. Mattoni said, that is something in the hands of arbitration counsel.

73 Another factor to be considered under section 11.4(2) is how the company's business and financial affairs are to be managed during the proceedings. In my view, the management of the business and affairs of Crystallex under the provisions discussed, being the conduct of the arbitration and paying for it, are a reasonable compromise between Crystallex and Tenor designed to protect the interests of the stakeholders, including the noteholders. The Monitor, of course, will continue to have an important role to play as well in the oversight of matters. If the noteholders are unhappy with the expenditures for the arbitration claim being incurred in the future, and there is no indication so far that they are, they have the ability in the CCAA process to object to them.

74 The noteholders also contend that because a term of default of the Tenor loan is a refusal of the court to extend the section 11 stay, that term ties the court's hands on any stay extension application, thus creating an incentive for Crystallex not to bargain towards a consensual resolution. I do not accept that the court's hands will be tied in any way. One would expect in any CCAA case that on a refusal to extend the stay, a DIP lender's loan would become payable. This provision in the Tenor loan is not remarkable.

75 The noteholders make the same point about it being a term of default of the Tenor loan if the CCAA case is converted to a receivership, a proposal in bankruptcy or bankruptcy proceeding. Again, one would expect a DIP loan to become payable in these events. This is a normal provision in a DIP loan, as conceded by Mr. Swan in argument. If bankruptcy were appropriate, this provision would not prevent it.

76 The noteholders contend that the right of Tenor to 35% of the proceeds of the arbitration, convertible into equity at Tenor's discretion, should not occur as it will hamper any ability to reach

any restructuring resolution. In the bid procedures approved by the Monitor, the market was told that any "back-end entitlement" could not exceed 49% of the equity of Crystallex. 35% is a very large block of the arbitration proceeds and obviously Crystallex would not have been happy to give that up. It eats into any recovery for the shareholders who are entitled to receive any proceeds of the arbitration only after the noteholders have been paid in full. However, 35% on the record does not appear excessive. The process undertaken by Mr. Skatoff indicates that the terms of the Tenor bid were the result of a reasonable market search. Mr. Sauntry, the financial expert for the noteholders, could not say that the Tenor bid did not reflect market pricing. He also said on cross-examination that a return of 10% PIK interest would not be a reasonable return for DIP lender in this case because of the uncertainty of getting anything because of the arbitration risk and risk of collecting on any award, and that a lender would require some additional amount such as the 35% to make it a reasonable deal.

77 The noteholders propose in their proposed plan that they receive 23% of equity for their infusion of the $36 million needed for the arbitration claim. There is no evidence as to how that 23% figure was arrived at. However, the plan also provides for the noteholders to be given approximately 58% of the equity in return for giving up their notes. Together this amounts to 81% of the equity, and it is artificial to say that the 23% for the $36 million infusion reflects a market indication of the value of the infusion. I realize that the plan of the noteholders is only a proposal, but it does reflect a recognition that someone financing the arbitration would require a considerable amount of any arbitration award in order to take the risk of financing it. If the 35% figure in the Tenor DIP facility is used by the noteholders for the $36 million infusion (which the noteholders say they would be prepared to lend for 35% of the equity if later required), the amount of equity to the noteholders in their plan in return for their notes would be 46% rather than 58%, indicating an interest in receiving that amount of equity for their notes. If the Tenor DIP facility is accepted, it would leave 65% of the equity available, less 10% if the MIP is approved, more than the noteholders propose in their plan.

78 The noteholders also rely on a statement in Mr. Sauntry's expert report that the Tenor DIP proposal will prevent any plan of arrangement. He states:

> The Tenor DIP Proposal will prevent any plan of arrangement. In fact, it is the logical conclusion of a negotiation between the Company, which has stated that it does not want a CCAA plan prior to an Award or settlement arising from the Arbitration Claim, and Tenor, which may benefit from the Company's near-complete lack of flexibility, if future amendments are required.

79 Much of Mr. Sauntry's report is little more than legal argument in the guise of an expert's opinion. I view a good deal of his report in much the same light as Farley J. did of an expert report of Mr. Dennis Belcher in *Re Royal Oak Mines Inc*. (1999) 7 C.B.R. (4th) 293, in which he stated "Mr. Belcher has set forth in essence his view of the CCAA situation; he should be regarded as a powerful advocate ..." I see Mr. Sauntry being an advocate for the noteholders.

80 Some things fundamental to Mr. Sauntry's report are wrong. For example, he states that "This is a situation where a material asset could be sold to provide a significant recovery for creditors" and "It is demonstrably possible to sell a significant interest in the Company's business (i.e. the Arbitration Claim) for material proceeds." On cross-examination he acknowledged his understanding that the claim is not assignable. I have earlier referred to problems I have with Mr. Sauntry's attempts to value the arbitration claim.

81 I do not see the Tenor DIP facility preventing a plan of arrangement. The noteholders have no right to keep Crystallex's assets and equity static for the purposes of a plan of arrangement, so long as the DIP loan meets the criteria required for approval. The provisions in the Tenor DIP facility complained of are the result of market forces, and unless there is some other preferable DIP available, which for reasons I will deal with is not the case, the question is whether the Tenor DIP facility should be approved.

82 Reliance is placed by the noteholders on provisions of section 7.19 of the Tenor bid. It provides that Crystallex shall not without the consent of Tenor enter into an agreement with the noteholders that contains certain provisions, including:

(a) Paying any money to pre-filing creditors before Crystallex pays Tenor. The noteholders contend that this eliminated any realistic possibility of Crystallex being refinanced prior to the collection of an arbitral award or settlement. However, this is a normal provision in any DIP financing. Moreover, there is no realistic possibility of Crystallex being refinanced before an arbitration award or settlement, as previously discussed.

(b) Increasing interest payable to the pre-filing creditors above 15%. The reason for this provision was because under the Tenor bid, any post-filing interest to be paid to creditors is to be paid before the additional compensation of 35% is paid to Tenor, and Tenor negotiated to limit this amount. It perhaps is to be noted that on any bankruptcy of Crystallex, interest to the noteholders would be limited to 5%.

(c) Issuing any equity containing anti-dilution provisions, which the noteholders contend means that any new equity proposed to be issued as a compromise exchange for debt could immediately thereafter be completely devalued at the next moment. I am not clear why this was negotiated by Tenor. In reply Mr. Kent contended that the problem could be taken care of by issuing shares to the noteholders with a coupon or agreement that would lock in their right to a percentage of the arbitration award. As the equity in Crystallex is essentially the same as the proceeds of the arbitration, presumably this is something that could be taken care of in a plan. Whether Crystallex would ever attempt to later issue equity to a third party is of course completely unknown and speculative, but it were to be contemplated during the course of the CCAA proceedings, presumably the

> Monitor would be aware of it and it would become known to the noteholders who would be able to apply to court for any appropriate relief.

83 I have previously discussed much of what is to be considered under s. 11.4 of the CCAA. Regarding (d), whether the loan would enhance the prospects of a viable compromise or arrangement, in my view it would. Crystallex requires additional financing to pay its expenses and continue the arbitration. A DIP loan allows the company to have the arbitration financed, which if it were not at this stage would impair the arbitration and perhaps the attitude of Venezuela towards the arbitration claim, and as such enhances the viability of a CCAA plan. I have not accepted the argument of the noteholders that the loan would prevent a plan of arrangement.

84 Regarding (f), whether any creditor would be materially prejudiced by the security, the noteholders are unhappy with the Tenor bid and say they are materially prejudiced, for the reasons that I have discussed and largely rejected. I think their complaints have to be looked at in the context of what the market is demanding for a DIP loan. There was a sufficient arm's length and open effort by Crystallex with the assistance of the Monitor to get the best pricing and terms for the loan and the process was carried out with integrity and fairness. The noteholders were asked during the process to increase their proposal but refused to do so. When at the last moment they indicated they would if later required lend on the same terms as the Tenor DIP facility, they made clear they would not agree to do so at this time. That, of course, is their choice. In all of the circumstances, I would not find that they have been materially prejudiced.

(ii) Consideration of the noteholders' proposed DIP facility

85 The noteholders' proposed DIP loan is for $10 million at 1% interest repayable on October 15, 2012. The term is said to give sufficient time to work out a plan of arrangement or compromise. Mr. Swan said in argument that the noteholders were not being altruistic in this proposal, but merely wanted to maintain the status quo while a plan is being negotiated.

86 The problem that the board of Crystallex had with this proposal was based on the advice of Mr. Skatoff. He advised the board that if Crystallex needed additional financing in October 2012, it would be difficult to return to the market for financing because there was only so much time and energy that bidders were willing to devote to a transaction. Having devoted the time and failed, bidders would be highly reluctant to spend additional time again. In his affidavit, Mr. Skatoff stated that if Crystallex accepted the $10 million DIP financing it would be highly challenged if not entirely impeded in any subsequent exercise to raise additional financing from parties other than the noteholders.

87 The noteholders contend that Mr. Skatoff's views on the difficulty of any future financing if the noteholders' proposed DIP loan is approved is "complete puffery" as he said on cross-examination that the parties with whom he negotiated never told him that they would absolutely not participate in a financing in the fall of 2012 if it were necessary. I think this is oversimplification and I do not accept it. Mr. Skatoff also said on cross-examination-

> I know what the facts are in terms of the financing market and how it views Crystallex. ... I believe that the company, if it were to accept a $10,000,000 financing, would need to go to the market in the very near term to start to address what happens if that $10,000,000 needed to be refinanced when ... we reached October of 2012. And I believe in the construct of my experience with this situation over the last three months that if the company were to accept that $10,000,000, we would need to go back out to the market in the very near term to raise capital to possibly refinance that money in the event that $10,000,000 couldn't be extended, that the company would have a very difficult time in convincing potential financing parties to undertake to spend additional time and resources in evaluating potential financing, as we have been able to convince them to do over the last couple months.

88 I accept that evidence as reliable. Common sense would indicate that persons who spent time and energy on pursuing a $36 million facility for a three year term only to see a 6 month facility for $10 million being accepted would be very reluctant to go through the process again in the next few months.

89 This is particularly the case, in my view, when the proposed interest rate by the noteholders is only 1%, clearly below the market rate.[3] The market would see that rate, as would any reasonable observer, as being used for some purpose to further the ends of the noteholders. Hedge funds are not in the business of lending money at less than market rates. The rate no doubt was proposed to assist an argument that the court should accept the noteholders' proposed loan. Why would the noteholders propose that? The answer, I believe, is that it would assist in removing, or seriously eroding, the chance of Crystallex going to the market in time for a new loan by October and thus further make Crystallex beholden to the noteholders in October, as stated by Mr. van't Hof and Mr. Skatoff. I do not view the noteholders proposed loan as being a *bona fide* loan at market rates but rather a loan to gain tactical advantage.

90 Thus, I do not see the noteholders proposed $10 million 1% six month facility as maintaining the status quo. I accept the evidence of Mr. Skatoff that it would seriously erode the chances of Crystallex obtaining any third party financing in October.

91 Had the noteholders been prepared to lend now on the basis of the terms of the Tenor DIP facility, that would have been a preferable outcome, even if it was not made within the terms of the bid process approved by the Monitor, as it would not have involved the insertion of any third party into the process. Unfortunately, it was made clear during argument that the noteholders were not prepared at this time to do so. The uncertainty of a short six month loan when it is clear that financing for a much longer term is required by Crystallex to prosecute the arbitration is something to be avoided.

(iii) Position of the Monitor

92 I have previously referred to portions of the Monitor's report. The Monitor concludes that on the basis that Crystallex, with assistance of Mr. Skatoff, conducted a canvas of the market and determined that the Tenor Bid was the best available bid generated out of the process to meet its objectives, the Monitor supports approval of the Tenor DIP Loan. This position of the Monitor is subject to this court's determination of the validity of the noteholders' legal arguments, on which the Monitor expresses no view as these are legal issues to be determined by the Court.

93 It is the case, as the Monitor points out, that the introduction of a third party, Tenor, with consent rights to certain actions will add complexity to the negotiation of a CCAA plan. I entirely agree with the Monitor that a mutually acceptable CCAA plan is preferable to continued expensive and protracted legal disputes between the Noteholders and Crystallex. However, in spite of the encouragement of the Monitor and of the court over the last while to see if a settlement could be reached, that has unfortunately not occurred.

(iv) Conclusion on DIP loan

94 Taking into account all of the forgoing, I approve the Tenor DIP facility.

(v) Request for stay

95 The noteholders ask that in the event that the Tenor DIP facility is approved, the order should be stayed pending an appeal to the Court of Appeal. The parties have already had discussion through the Monitor with the Court of Appeal which has agreed as I understand it to move as expeditiously as possible with any appeal from my decision.

96 A judge whose decision is to be appealed can stay the order on such terms as are just. On motions for stays, courts apply the *RJR Macdonald* test and will order stays in restructuring and insolvency proceedings to allow sufficient to for consideration of an appeal.

97 At first blush during the argument, I was inclined to agree with the noteholders that a stay would be appropriate pending an appeal, assuming that it could be dealt with expeditiously. However, argument from Crystallex gave me pause, particularly when the cash flow needs of Crystallex are considered. The cash flow projections as shown in the Monitor's report indicate that as of the end of the week ending April 13, 2012, Crystallex had only $346,000, and that during the following week, it had cash requirements of approximately $6 million, including repayment of the bridge loan due on April 16. Crystallex does not have the luxury of waiting for the conclusion of a successful appeal.

98 The answer of the noteholders to this was that the problem would be solved if the court approved its $10 million DIP proposal rather than the Tenor bid. I understand that the noteholders would be prepared to lend the $10 million if an appeal to the Court of Appeal from an order approving the Tenor DIP facility were successful.

99 Under the Tenor DIP facility, the right of Tenor to the additional compensation of 35% of the proceeds of the arbitration does not arise until the second tranche of the loan of $12 million has been advanced, and this is not due until after any appeal to the Court of Appeal has been completed. As to concerns of the noteholders that Tenor might pre-pay the second tranche in order to fix its right to the additional compensation, I was advised during argument that Tenor has undertaken not to do so and Crystallex has undertaken as well not to draw on the second tranche without two weeks' notice to the noteholders.

100 Crystallex, and I assume Tenor as well, has agreed that pending the completion of an appeal to the Court of Appeal, the right of Tenor to convert its rights to 35% of the arbitration proceeds and the governance provisions for Crystallex would also be stayed.

101 In my view, and assuming that the first test of *RJR Macdonald* has been met, there should be no stay of my order approving the Tenor DIP facility, and this can be done in a manner that will protect the interests of the parties on the following basis:

(i) The order approving the Tenor DIP facility shall be subject to the undertakings and agreements of Crystallex and Tenor as referred to.

(ii) The Tenor DIP facility is approved on condition that in the event that the appeal to the Court of Appeal is successful, and the order approving the Tenor DIP facility is set aside in its entirety, the money advanced by Tenor on the first tranche shall be immediately repayable with interest at 1% per annum, in which case the Tenor DIP facility shall be terminated. Tenor shall have no right in that case to any commitment fee which, if already paid, shall be deducted from the repayment of the loan to Tenor.

(iii) The noteholders shall in that event fund the repayment to Tenor by loan to Crystallex with interest at $1% per annum repayable on October 15, 2012 or at some other date as may be agreed or ordered by this court.

Management Incentive Plan (MIP)

102 The terms of the MIP are set out above. In sum, a pool of money, consisting of up to 10% of the net proceeds of the arbitration up to $700 million and 2% of any further net proceeds, after all costs and charges, including the amounts owing to noteholders, is to be set aside and money in this pool may be paid to the beneficiaries of the MIP, depending on the determination of an independent committee. The amounts to be allocated to participants by the compensation committee are discretionary and could be nil. No one will be entitled to any particular amount. Members of the compensation committee will not be eligible for any payments.

103 In exercising its discretion to consider whether and in what amount a payment should be made, the compensation committee will take the following factors into account:

(a) The amount of money recovered by Crystallex in the arbitration.
(b) The risks affecting the size of the retention pool including the quantum of the priority payments and the fact that others have influence on discussions relating to the settlement of the claim
(c) How quickly the funds are recovered.
(d) The impact the premature resignation of the individual from Crystallex would or could have had upon the results of the arbitration.
(e) The amount of time and energy spent by the individual on the arbitration.
(f) [Certain matters confidential to the parties.]
(g) The scale and scope of the balance of the compensation package provided by Crystallex to the individual.
(h) The opportunity cost to the individual in staying with Crystallex in terms of professional experience, money and the development of new opportunities.
(i) The amount of any severance payments the employee would receive on termination if such termination is reasonably foreseeable and will be accompanied by a severance payment.
(j) The extent to which the arbitration cost more than anticipated to prosecute and the degree to which it may be appropriate to reduce the bonus pool as a result.
(k) Any other relevant matter.

104 The noteholders disagree with Crystallex on the quantum and method for providing an incentive to management. They have also expressed concerns as to the timing of the MIP approval motion and inclusion of some MIP participants in the MIP. Under their proposed plan, management would receive 5% through an equity participation in any after tax award.

105 The Tenor DIP loan is conditional on the approval of a management incentive program acceptable to both Tenor and Crystallex. Tenor has not voiced any objection to the MIP proposal of Crystallex and I take it is in agreement with it. The requirement for a management incentive program acceptable to Tenor is a reflection, obviously, of the need to ensure the participation of the people necessary to pursue the arbitration to a satisfactory conclusion.

106 The reasons for the MIP are set out in the affidavit of Mr. van't Hof. See paras. 4 to 10 and 14 to 23 of his affidavit. In the circumstances of this arbitration, these reasons appear legitimate. They were considered so by the independent directors of Crystallex constituting the compensation committee and by Mr. Jay Swartz of Davies Ward Phillips & Vineberg LLP.

107 Mr. van't Hof states in his affidavit that because in past litigation the noteholders have criticized the independent directors of Crystallex as not being sufficiently independent because of prior business relationships with Robert Fung or companies with which Mr. Fung was associated, Crystallex retained Jay Swartz, a partner of Davies Phillips Vineberg, to determine, from the

perspective of an independent director, what an appropriate MIP would be. In coming to that determination, Mr. Swartz was told he could retain such advisors as he saw fit and take such steps as he saw fit. Mr. Swartz' opinion of March 14, 2012 states that he was engaged on June 6, 2011 to negotiate the terms on which directors and members of management will be compensated for their ongoing duties. With the consent of Crystallex, Mr. Swartz retained Hugessen Consulting Inc., an independent national executive compensation consulting firm to provide expert advice with respect to compensation issues and to provide background information regarding compensation standards in circumstances which were analogous to the issues facing Crystallex. Mr. Swartz reviewed extensive documentation and carried out extensive discussions with various persons including the solicitors for Crystallex, counsel for the board and with Freshfields who are arbitration counsel.

108 Mr. Swartz concluded that the overall compensation proposal for the establishment of the bonus pool for the benefit of management of Crystallex was reasonable in the circumstances, for reasons expressed in his opinion. Included in his reasons was the following:

> The current members of the Compensation Committee are granted substantial discretion to allocate, or not allocate, the bonus Pool and can do so in their discretion having regard to what actually occurs over time and the relative and absolute contributions of each party. In doing so, they are subject to fiduciary duties to Crystallex. In this regard, I note that there may be circumstances when the absolute amount of the bonus Pool may be very substantial in light of all of the factors to be considered by the Compensation Committee. In such circumstances, the Compensation Committee may have to carefully consider the absolute amounts to be paid to each member of a Management Group in order to satisfy its fiduciary duties.

109 Whether KERP provisions such as the ones in this case should be ordered in a CCAA proceeding is a matter of discretion. While there are a small number of cases under the CCAA dealing with this issue, it certainly cannot be said that there is any established body of case law settling the principles to be considered. In *Houlden & Morawetz Bankruptcy and Insolvency Analysis*, West Law, 2009, it is stated:

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

110 In *Canadian Insolvency in Canada* by Kevin P. McElcheran (LexisNexis -- Butterworths) at p. 231, it is stated:

> KERPs and special director compensation arrangements are heavily negotiated

> and controversial arrangements. ... Because of the controversial nature of KERP arrangements, it is important that any proposed KERP be scrutinized carefully by the monitor with a view to insisting that only true key employees are covered by the plan and that the KERP will not do more harm than good by failing to include the truly key employees and failing to treat them fairly.

111 In *Re Grant Forest Products Inc*. (2009), 57 C.B.R. (5th) 128, I accepted these statements as generally being applicable to motions to approve key employee retention plans. See also *Re Canwest Global Communications Corp*. (2009), 59 C.B.R. (5th) 72, *Re Nortel Networks Corporation*, [2009] O.J. No. 1044, *Re Canwest Publishing Inc*., (2010), 63 C.B.R. (5th) 115 and *Re Timminco Ltd*. [2012] O.J. No. 472.

112 I see no reason why the business judgment rule is not applicable, particularly when the provisions of the MIP have been approved by an independent committee of the board. See my comments in *Grant Forest Products*, in which the payments in question were approved by an independent committee of the board of the debtor, in which I said that the business judgment of the directors should rarely be ignored. See also Morawetz J. in *Re Timminco.*

113 In this case, the qualifications of the independent board members, Messrs. Brown, Near and van't Hof, are impressive, and these people are non-conflicted as they will not participate in the MIP. They acted on advice from Mr. Swartz and had market information from Mr. Skatoff as noted in paras. 10 and 33 of Mr. van't Hof's affidavit. Their judgment was informed and I am in no position to say it was unreasonable.

114 There is no question that the judgment of Mr. Swartz is independent and informed, and I would not lightly ignore it without good reason.

115 The noteholders contend that the MIP is something that should await the negotiations of a plan. I can understand the logic of that position, particularly when as here the MIP is to be funded from the proceeds of the arbitration, which is the "asset" that will be the subject of the negotiations of a plan, whether that asset is called the proceeds of the arbitration or equity. However, I am hesitant to have the uncertainty of such a situation hanging over the heads of the people meant to be protected by the MIP. In *Grant Forest Products*, over the objection of a substantial creditor, and in *Canwest Global, Canwest Publishing* and *Timminco*, employee retention plans were approved prior to any plan being negotiated, and it appears to be the practice today that these types of plans are generally approved at the time of the initial orders.

116 The noteholders do not contend that there should not be any MIP. As the Monitor's report notes, under the noteholders' proposed plan, management would receive 5% through an equity participation in any after tax award. While the numbers between the Crystallex MIP (a pool of up to 10% of an award up to $700 million and 2% over that) and the noteholders plan (5%) are different, it is possible that the end result would not be different depending on what the independent compensation committee decided to allocate after the results of the arbitration were known.

117 The noteholders contend that there are participants in the MIP that should not belong. That is a matter of judgment, and the independent committee has exercised its judgment on the matter. The participants were also known to Mr. Swartz who opined as to the reasonableness of the principles of the MIP. Having reviewed the evidence, including the affidavit of Mr. van't Hof and of Ms. Kwinter, I cannot say that any of the persons included in the MIP should not be there.

118 Mr. Tony Reyes is a shareholder of Crystallex. He in principle is supportive of the MIP. He raises two concerns regarding the MIP.

119 The first is the fact that some of the persons who may benefit already have stock options and it is not clear that the proposed MIP will replace and cancel those options. Thus, these persons could end up with more than the MIP proposes. In response to this, Crystallex advises that it will amend the MIP to provide that the value of any existing stock options ultimately realized by participants of the MIP will be deducted from the amount of any bonus awarded under the MIP on a tax neutral basis.

120 The second relates to the method of calculating the bonus pool. It is described by the Monitor as follows:

> 83. Mr. Reyes also raises a concern that the MIP treats the creation of and payment out of the MIP Pool as a secured debt and not an equity distribution. The MIP Pool is to be protected by a Court-ordered charge and will be created out of the net proceeds of the Arbitration Proceedings but before any payment to shareholders. Value to shareholders is after the repayment of the additional compensation to Tenor and the MIP, while the MIP is calculated based on the gross award before repayment of additional compensation. He notes that the method of calculating the MIP Pool also serves to increase the potential effective "equity participation" of the pool participants well above the rate of 10% relative to the participation rate of existing shareholders, to an effective rate of 18% or more. This is due to the dilutive effect of Tenor's additional compensation on existing shareholders.

121 The first sentence regarding this concern is not correct. The MIP is triggered by a receipt of funds, and the charge over that pool does not give any priority to the participants in the MIP. Regarding the remainder of the concern, it seems to me that this is something that could be taken into account by the compensation committee in determining what, if any, amount should be allocated to any particular person.

122 The Monitor has reviewed the MIP and the noteholders proposal. The Monitor does not expressly state that it supports the MIP as proposed by Crystallex being approved, but clearly does not oppose it. Monitor concludes:

> 130. The MIP is ancillary to the Tenor DIP Loan and approval of a management

> incentive program is a condition of the Tenors DIP Loan. The Noteholders and Mr. Reyes appear to accept the Company's position that a substantial incentive plan is appropriate in these unique circumstances. Mr Swartz, from the perspective of the independent director with advice from Hugessen Consulting Inc., concludes that the Applicant's proposed MIP is "reasonable in the circumstances". The Noteholders and Mr. Reyes' position, however, is that the terms of any incentive plan should be less favourable to the participants than the MIP proposed by Crystallex.
>
> 131. Although the percentage amounts and debt structure provide the potential for compensation to management that could be substantial, both relative to the recoveries of other stakeholders and in absolute dollar terms, it is subject to the discretion of the independent directors who have fiduciary duties that will provide a measure of balance in the implementation of the MIP.

123 Like the DIP issue, it is unfortunate that Crystallex and the noteholders have not been able to come to some agreement on an MIP. It would have been far more preferable for that to have occurred. However there has been no agreement and it falls for decision by the court.

124 In all of the circumstances, as discussed, I approve the MIP proposed by Crystallex with the changes regarding the stock options agreed to by Crystallex.

Approval of Monitor's reports

125 Approval is sought of the actions of the Monitor as disclosed in its second and third report. I have no hesitation in approving these actions. A Monitor plays a crucial role in any CCAA restructuring, and this is particularly so in this case. The Monitor is to be commended for the way in which it has participated and in its efforts to bring a consensual resolution of matters as they have arisen. This assistance is invaluable. I approve the actions of the Monitor as set out in its second and third report.

Continuation of the stay

126 Crystallex seeks a continuation of the stay until July 16, 2012 or such further date as may be ordered. No one opposes the stay to that date, and it is supported by the Monitor who recommends the continuation. Due to holiday considerations, I continue the stay to July 30, 2012.

F.J.C. NEWBOULD J.

1 The noteholders in question are hedge funds that represent approximately 77% of the outstanding notes. It is they who have caused Computershare to take action on their behalf in the prior actions against Crystallex and in this CCAA proceeding.

2 The fact that the noteholders have an opinion questioning some of what Freshfields says does not change that.

3 The Monitor calculates the savings in interest over the Tenor loan to October 15, 2012 to be approximately $300,000.

TAB 4

2 of 4 DOCUMENTS

In the Matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended and in the Matter of a Proposed Plan of Compromise or Arrangement with respect to Stelco Inc., and other Applicants listed in Schedule "A" Application under the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 as amended

[Indexed as: Stelco Inc. (Re)]

75 O.R. (3d) 5

[2005] O.J. No. 1171

Docket: M32289

Court of Appeal for Ontario,

Goudge, Feldman and Blair JJ.A.

March 31, 2005

Corporations -- Directors -- Removal of directors -- Jurisdiction of court to remove directors -- Restructuring supervised by court under Companies' Creditors Arrangement Act -- Supervising judge erring in removing directors based on apprehension that directors would not act in best interests of corporation -- In context of restructuring, court not having inherent jurisdiction to remove directors -- Removal of directors governed by normal principles of corporate law and not by court's authority under s. 11 of Companies' Creditors Arrangement Act to supervise restructuring -- Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.

Debtor and creditor -- Arrangements -- Removal of directors -- Jurisdiction of court to remove directors -- Restructuring supervised by court under the Companies' Creditors Arrangement Act -- Supervising judge erring in removing directors based on apprehension that directors would not act in best interests of corporation - In context of restructuring, court not having inherent jurisdiction to remove directors -- Removal of directors governed by normal principles of corporate law and not by court's authority under s. 11 of Companies' Creditors Arrangement Act to supervise restructuring -- Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.

On January 29, 2004, Stelco Inc. ("Stelco") obtained protection from creditors under the Companies' Creditors Arrangement Act ("CCAA"). Subsequently, while a restructuring under the CCAA was under way, Clearwater Capital Management Inc. ("Clearwater") and Equilibrium Capital Management Inc. ("Equilibrium") acquired a 20 per cent holding in the outstanding publicly traded common shares of Stelco. Michael Woollcombe and Roland Keiper, who were associated with Clearwater and Equilibrium, asked to be appointed to the Stelco board of directors, which had been depleted as a result of resignations. Their request was supported by other shareholders who, together with Clearwater and Equilibrium, represented about 40 per cent of the common shareholders. On February 18, 2005, the Board acceded to the request and Woollcombe and Keiper were appointed to the Board. On the same day as their appointments, the board of directors began consideration of competing bids that had been received as a result of a court-approved capital raising process that had become the focus of the CCAA restructuring.

The appointment of Woollcombe and Keiper to the Board incensed the employees of Stelco. They applied to the court to have the appointments set aside. The employees argued that there was a reasonable apprehension that Woollcombe [page6] and Keiper would not be able to act in the best interests of Stelco as opposed to their own best interests as shareholders. Purporting to rely on the court's inherent jurisdiction and the discretion provided by the CCAA, on February 25, 2005, Farley J. ordered Woollcombe and Keiper removed from the Board.

Woollcombe and Keiper applied for leave to appeal the order of Farley J. and if leave be granted, that the order be set aside on the grounds that (a) Farley J. did not have the jurisdiction to make the order under the provisions of the CCAA, (b) even if he did have jurisdiction, the reasonable apprehension of bias test had no application to the removal of directors, (c) he had erred in interfering with the exercise by the Board of its business judgment in filling the vacancies on the Board, and (d) in any event, the facts did not meet any test that would justify the removal of directors by a court.

Held, leave to appeal should be granted, and the appeal should be allowed.

The appeal involved the scope of a judge's discretion under s. 11 of the CCAA, in the context of corporate governance decisions made during the course of the plan negotiating and approval process of the CCAA. In particular, it involved the court's power, if any, to make an order removing directors under s. 11 of the CCAA. The order to remove directors could not be founded on inherent jurisdiction. Inherent jurisdiction is a power derived from the very nature of the court as a superior court of law, and it permits the court to maintain its authority and to prevent its process from being obstructed and abused. However, inherent jurisdiction does not operate where Parliament or the legislature has acted and, in the CCAA context, the discretion given by s. 11 to stay proceedings against the debtor corporation and the discretion given by s. 6 to approve a plan which appears to be reasonable and fair supplanted the need to resort to inherent jurisdiction. A judge is general ly exercising the court's statutory discretion under s. 11 of the Act when supervising a CCAA proceeding. The order in this case could not be founded on inherent jurisdiction because it was

designed to supervise the company's process, not the court's process.

The issue then was the nature of the court's power under s. 11 of the CCAA. The s. 11 discretion is not open-ended and unfettered. Its exercise was guided by the scheme and object of the Act and by the legal principles that govern corporate law issues. What the court does under s. 11 is establish the boundaries of the playing field and act as a referee in the process. The company's role in the restructuring, and that of its stakeholders, is to work out a plan or compromise that a sufficient percentage of creditors will accept and the court will approve and sanction. In the course of acting as referee, the court has authority to effectively maintain the status quo in respect of an insolvent company while it attempts to gain the approval of its creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors. The court is not entitled to usurp the role of the directors and management in conducting what are in substance the company's restructurin g efforts. The corporate activities that take place in the course of the workout are governed by the legislation and legal principles that normally apply to such activities. The court is not catapulted into the shoes of the board of directors or into the seat of the chair of the board when acting in its supervisory role in the restructuring.

The matters relating to the removal of directors did not fall within the court's discretion under s. 11. The fact that s. 11 did not itself provide the authority for a CCAA judge to order the removal of directors, however, did not mean that the supervising judge was powerless to make such an order. Section 20 of the CCAA offered a gateway to the oppression remedy and other provisions of the Canada [page7] Business Corporations Act, R.S.C. 1985, c. C-44 ("CBCA") and similar provincial statutes. The powers of a judge under s. 11 of the CCAA may be applied together with the provisions of the CBCA, including the oppression remedy provisions of that statute.

Court removal of directors is an exceptional remedy and one that is rarely exercised in corporate law. In determining whether directors have fallen foul of their obligations, more than some risk of anticipated misconduct is required before the court can impose the extraordinary remedy of removing a director from his or her duly elected or appointed office. The evidence in this case was far from reaching the standard for removal, and the record would not support a finding of oppression, even if one had been sought. The record did not support a finding that there was a sufficient risk of misconduct to warrant a conclusion of oppression. Further, Farley J.'s borrowing the administrative law notion of apprehension of bias was foreign to the principles that govern the election, appointment and removal of directors and to corporate governance considerations in general. There was nothing in the CBCA or other corporate legislation that envisaged the screening of directors in advance for their ability to a ct neutrally, in the best interests of the corporation, as a prerequisite for appointment. The issue to be determined was not whether there was a connection between a director and other shareholders or stakeholders, but rather whether there was some conduct on the part of the director that would justify the imposition of a corrective sanction. An apprehension of bias approach did not fit this sort of analysis.

For these reasons, Farley J. erred in declaring the appointment of Woollcombe and Keiper as

directors of Stelco of no force and effect, and the appeal should be allowed.

Cases referred to

Alberta Pacific Terminals Ltd. (Re), [1991] B.C.J. No. 1065, 8 C.B.R. (3d) 99 (S.C.); Algoma Steel Inc. (Re), [2001] O.J. No. 1943, 147 O.A.C. 291, 25 C.B.R. (4th) 194 (C.A.); Algoma Steel Inc. v. Union Gas Ltd. (2003), 63 O.R. (3d) 78, [2003] O.J. No. 71, 39 C.B.R. (4th) 5 (C.A.), revg in part [2001] O.J. No. 5046, 30 C.B.R. (4th) 163 (S.C.J.); Babcock & Wilcox Canada Ltd. (Re) [2000] O.J. No. 786, 18 C.B.R. (4th) 157, 5 B.L.R. (3d) 75 (S.C.J.); Baxter Student Housing Ltd. v. College Housing Co-operative Ltd., [1976] 2 S.C.R. 475, 57 D.L.R. (3d) 1, 5 N.R. 515, [1976] 1 W.W.R. 1, 20 C.B.R. (N.S.) 240; Blair v. Consolidated Enfield Corp., [1995] 4 S.C.R. 5, [1995] S.C.J. No. 29, 25 O.R. (3d) 480n, 128 D.L.R. (4th) 73, 187 N.R. 241, 24 B.L.R. (2d) 161; Brant Investments Ltd. v. KeepRite Inc. (1991), 3 O.R. (3d) 289, [1991] O.J. No. 683, 45 O.A.C. 320, 80 D.L.R. (4th) 161, 1 B.L.R. (2d) 225 (C.A.); Catalyst Fund General Partne r I Inc. v. Hollinger Inc., [2004] O.J. No. 4722, 1 B.L.R. (4th) 186 (S.C.J.); Chef Ready Foods Ltd. v. Hongkong Bank of Canada, [1990] B.C.J. No. 2384, 51 B.C.L.R. (2d) 84, [1991] 2 W.W.R. 136, 4 C.B.R. (3d) 311 (C.A.); Clear Creek Contracting Ltd. v. Skeena Cellulose Inc. [2003] B.C.J. No. 1335, 43 C.B.R. (4th) 187, 2003 BCCA 344, 13 B.C.L.R. (4th) 236 (C.A.); Country Style Foods Services Inc. (Re), [2002] O.J. No. 1377, 158 O.A.C. 30 (C.A.); Dylex Ltd. (Re), [1995] O.J. No. 595, 31 C.B.R. (3d) 106 (Gen. Div.); Ivaco Inc. (Re), [2004] O.J. No. 2483, 3 C.B.R. (5th) 33 (S.C.J.); Lehndorff General Partner Ltd. (Re), [1993] O.J. No. 14, 9 B.L.R. (2d) 275, 17 C.B.R. (3d) 24 (Gen. Div.); London Finance Corp. Ltd. v. Banking Service Corp. Ltd., [1922] O.J. No. 378, 23 O.W.N. 138 (H.C.); Olympia & York Developments Ltd. (Re) (1993), 12 O.R. (3d) 500, [1993] O.J. No. 545, 17 C.B.R. (3d) 1 (Gen. Div.) (sub nom. Olympia & York Dev. v. Royal Trust Co.); Peoples Department Stores Inc. (Trustee of) v. Wise, [2004] 3 S.C.R. 461, [2004] S.C.J. No. 64, 244 D.L.R. (4th) 564, 2004 SCC 68, 49 B.L.R. (3d) 165, 4 C.B.R. (5th) 215; R. v. Sharpe, [2001] 1 S.C.R. 45, [2001] [page8] S.C.J. No. 3, 88 B.C.L.R. (3d) 1, 194 D.L.R. (4th) 1, [2001] 6 W.W.R. 1, 86 C.R.R. (2d) 1, 150 C.C.C. (3d) 321, 39 C.R. (5th) 72, [2001] SCC 2; Richtree Inc. (Re) (2005), 74 O.R. (3d) 174, [2005] O.J. No. 251, 7 C.B.R. (5th) 294 (S.C.J.); Rizzo & Rizzo Shoes Ltd. (Re), [1998] 1 S.C.R. 27, [1998] S.C.J. No. 2, 36 O.R. (3d) 418n, 154 D.L.R. (4th) 193, 221 N.R. 241, 50 C.B.R. (3d) 163, 33 C.C.E.L. (2d) 173, 98 CLLC 210-006 (sub nom. Ontario Ministry of Labour v. Rizzo & Rizzo Shoes Ltd., Adrien v. Ontario Ministry of Labour); Royal Oak Mines Inc. (Re), [1999] O.J. No. 864, 7 C.B.R. (4th) 293, 96 O.T.C. 279 (Gen. Div.); Sammi Atlas Inc. (Re), [1998] O.J. No. 1089, 3 C.B.R. (4th) 171 (Gen. Div.); Stephenson v. Vokes (1896), 27 O.R. 691, [1896] O.J. No. 191 (H.C.J.); Westar Mining Ltd. (Re), [1992] B.C.J. No. 1360, 14 C.B.R. (3d) 88, 70 B.C.L.R. (2d) 6, [1992] 6 W.W.R. 331 (S.C.)

Statutes referred to

Canada Business Corporations Act, R.S.C. 1985, c. C-44, ss. 2 [as am.], 102 [as am.], 106(3) [as am], 109(1) [as am.], 111 [as am.], 122(1) [as am.], 145 [as am.], 241 [as am.]

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, ss. 11 [as am.], 20 [as am.]

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APPLICATION for leave to appeal and, if leave is granted, an appeal from the order of Farley J., reported at [2005] O.J. No. 729, 7 C.B.R. (5th) 307 (S.C.J.), removing two directors from the board of directors of Stelco Inc.

Jeffrey S. Leon and Richard B. Swan, for appellants Michael Woollcombe and Roland Keiper.

Kenneth T. Rosenberg and Robert A. Centa, for respondent United Steelworkers of America.

Murray Gold and Andrew J. Hatnay, for respondent Retired Salaried Beneficiaries of Stelco Inc., CHT Steel Company Inc., Stelpipe Ltd., Stelwire Ltd. And Welland Pipe Ltd.

Michael C.P. McCreary and Carrie L. Clynick, for USWA Locals 5328 and 8782.

John R. Varley, for Active Salaried Employee Representative.

Michael Barrack, for Stelco Inc.

Peter Griffin, for Board of Directors of Stelco Inc.

K. Mahar, for Monitor.

David R. Byers, for CIT Business Credit, Agent for DIP Lender. [page9]

The judgment of the court was delivered by

BLAIR J.A.: --

Part I -- Introduction

[1] Stelco Inc. and four of its wholly-owned subsidiaries obtained protection from their creditors under the Companies' Creditors Arrangement Act (the "CCAA")[1] at the end of the document] on January 29, 2004. Since that time, the Stelco Group has been engaged in a high profile, and sometimes controversial, process of economic restructuring. Since October 2004, the restructuring has revolved around a court-approved capital raising process which, by February 2005, had generated a number of competitive bids for the Stelco Group.

[2] Farley J., an experienced judge of the Superior Court Commercial List in Toronto, has been supervising the CCAA process from the outset.

[3] The appellants, Michael Woollcombe and Roland Keiper, are associated with two companies -- Clearwater Capital Management Inc. and Equilibrium Capital Management Inc. -- which, respectively, hold approximately 20 per cent of the outstanding publicly traded common shares of Stelco. Most of these shares have been acquired while the CCAA process has been ongoing, and Messrs. Woollcombe and Keiper have made it clear publicly that they believe there is good shareholder value in Stelco in spite of the restructuring. The reason they are able to take this position is that there has been a solid turn around in worldwide steel markets, as a result of which Stelco, although remaining in insolvency protection, is earning annual operating profits.

[4] The Stelco board of directors (the "Board") has been depleted as a result of resignations, and in January of this year Messrs. Woollcombe and Keiper expressed an interest in being appointed to the Board. They were supported in this request by other shareholders who, together with Clearwater and Equilibrium, represent about 40 per cent of the Stelco common shareholders. On February 18, 2005, the Board appointed the appellants directors. In announcing the appointments publicly, Stelco said in a press release:

> After careful consideration, and given potential recoveries at the end of the company's restructuring process, the Board responded favourably to the requests by making the appointments announced today.
>
> Richard Drouin, Chairman of Stelco's Board of Directors, said: "I'm pleased to welcome Roland Keiper and Michael Woollcombe to the Board. Their [page10] experience and their perspective will assist the Board as it strives to serve the best interests of all our stakeholders. We look forward to their positive contribution."

[5] On the same day, the Board began its consideration of the various competing bids that had been received through the capital raising process.

[6] The appointments of the appellants to the Board incensed the employee stakeholders of Stelco (the "Employees"), represented by the respondent Retired Salaried Beneficiaries of Stelco and the respondent United Steelworkers of America ("USWA"). Outstanding pension liabilities to current and retired employees are said to be Stelco's largest long-term liability -- exceeding several billion dollars. The Employees perceive they do not have the same, or very much, economic leverage in what has sometimes been referred to as "the bare knuckled arena" of the restructuring process. At the same time, they are amongst the most financially vulnerable stakeholders in the piece. They see the appointments of Messrs. Woollcombe and Keiper to the Board as a threat to their well being in the restructuring process because the appointments provide the appellants, and the shareholders they represent, with direct access to sensitive information relating to the competing bids to which other stakeholders (including themselves) are not privy.

[7] The Employees fear that the participation of the two major shareholder representatives will tilt the bid process in favour of maximizing shareholder value at the expense of bids that might be more favourable to the interests of the Employees. They sought and obtained an order from Farley J. removing Messrs. Woollcombe and Keiper from their short-lived position of directors, essentially on the basis of that apprehension.

[8] The Employees argue that there is a reasonable apprehension the appellants would not be able to act in the best interests of the corporation -- as opposed to their own best interests as shareholders -- in considering the bids. They say this is so because of prior public statements by the appellants about enhancing shareholder value in Stelco, because of the appellants' linkage to such a large shareholder group, because of their earlier failed bid in the restructuring, and because of their opposition to a capital proposal made in the proceeding by Deutsche Bank (known as the "Stalking Horse Bid"). They submit further that the appointments have poisoned the atmosphere of the restructuring process, and that the Board made the appointments under threat of facing a potential shareholders' meeting where the members of the Board would be replaced en masse. [page11]

[9] On the other hand, Messrs. Woollcombe and Keiper seek to set aside the order of Farley J. on the grounds that (a) he did not have the jurisdiction to make the order under the provisions of the CCAA, (b) even if he did have jurisdiction, the reasonable apprehension of bias test applied by the motion judge has no application to the removal of directors, (c) the motion judge erred in interfering with the exercise by the Board of its business judgment in filling the vacancies on the Board, and (d) the facts do not meet any test that would justify the removal of directors by a court in any event.

[10] For the reasons that follow, I would grant leave to appeal, allow the appeal and order the reinstatement of the applicants to the Board.

Part II -- Additional Facts

[11] Before the initial CCAA order on January 29, 2004, the shareholders of Stelco had last met at their annual general meeting on April 29, 2003. At that meeting they elected 11 directors to the Board. By the date of the initial order, three of those directors had resigned, and on November 30, 2004, a fourth did as well, leaving the company with only seven directors.

[12] Stelco's articles provide for the Board to be made up of a minimum of ten and a maximum of 20 directors. Consequently, after the last resignation, the company's corporate governance committee began to take steps to search for new directors. They had not succeeded in finding any prior to the approach by the appellants in January 2005.

[13] Messrs. Woollcombe and Keiper had been accumulating shares in Stelco and had been participating in the CCAA proceedings for some time before their request to be appointed to the Board, through their companies, Clearwater and Equilibrium. Clearwater and Equilibrium are privately held, Ontario-based investment management firms. Mr. Keiper is the president of Equilibrium and associated with Clearwater. Mr. Woollcombe is a consultant to Clearwater. The motion judge found that they "come as a package".

[14] In October 2004, Stelco sought court approval of its proposed method of raising capital. On October 19, 2004, Farley J. issued what has been referred to as the Initial Capital Process Order. This order set out a process by which Stelco, under the direction of the Board, would solicit bids, discuss the bids with stakeholders, evaluate the bids and report on the bids to the court.

[15] On November 9, 2004, Clearwater and Equilibrium announced they had formed an investor group and had made a [page12]capital proposal to Stelco. The proposal involved the raising of $125 million through a rights offering. Mr. Keiper stated at the time that he believed "the value of Stelco's equity would have the opportunity to increase substantially if Stelco emerged from CCAA while minimizing dilution of its shareholders." The Clearwater proposal was not accepted.

[16] A few days later, on November 14, 2004, Stelco approved the Stalking Horse Bid. Clearwater and Equilibrium opposed the Deutsche Bank proposal. Mr. Keiper criticized it for not providing sufficient value to existing shareholders. However, on November 29, 2004, Farley J. approved the Stalking Horse Bid and amended the Initial Capital Process Order accordingly. The order set out the various channels of communication between Stelco, the monitor, potential bidders and the stakeholders. It provided that members of the Board were to see the details of the different bids before the Board selected one or more of the offers.

[17] Subsequently, over a period of two and a half months, the shareholding position of Clearwater and Equilibrium increased from approximately five per cent as at November 19, to 14.9 per cent as at January 25, 2005, and finally to approximately 20 per cent on a fully diluted basis as at January 31, 2005. On January 25, Clearwater and Equilibrium announced that they had reached an understanding jointly to pursue efforts to maximize shareholder value at Stelco. A press release stated:

> Such efforts will include seeking to ensure that the interests of Stelco's equity holders are appropriately protected by its board of directors and, ultimately, that Stelco's equity holders have an appropriate say, by vote or otherwise, in determining the future course of Stelco.

[18] On February 1, 2005, Messrs. Keiper and Woollcombe and other representatives of Clearwater and Equilibrium met with Mr. Drouin and other Board members to discuss their views of Stelco and a fair outcome for all stakeholders in the proceedings. Mr. Keiper made a detailed presentation, as Mr. Drouin testified, "encouraging the Board to examine how Stelco might improve its value through enhanced disclosure and other steps". Mr. Keiper expressed confidence that "there was value to the equity of Stelco", and added that he had backed this view up by investing millions of dollars of his own money in Stelco shares. At that meeting, Clearwater and Equilibrium requested that Messrs. Woollcombe and Keiper be added to the Board and to Stelco's restructuring committee. In this respect, they were supported by other shareholders holding about another 20 per cent of the company's common shares. [page13]

[19] At paras. 17 and 18 of his affidavit, Mr. Drouin, summarized his appraisal of the situation:

> 17. It was my assessment that each of Mr. Keiper and Mr. Woollcombe had personal qualities which would allow them to make a significant contribution to the Board in terms of their backgrounds and their knowledge of the steel industry generally and Stelco in particular. In addition I was aware that their appointment to the Board was supported by approximately 40 per cent of the shareholders. In the event that these shareholders successfully requisitioned a shareholders meeting they were in a position to determine the composition of the entire Board.
> 18. I considered it essential that there be continuity of the Board through the CCAA process. I formed the view that the combination of existing Board members and these additional members would provide Stelco with the most appropriate board composition in the circumstances. The other members of the Board also shared my views.

[20] In order to ensure that the appellants understood their duties as potential Board members and, particularly that "they would no longer be able to consider only the interests of shareholders alone but would have fiduciary responsibilities as a Board member to the corporation as a whole", Mr. Drouin and others held several further meetings with Mr. Woollcombe and Mr. Keiper. These discussions "included areas of independence, standards, fiduciary duties, the role of the Board Restructuring Committee and confidentiality matters". Mr. Woollcombe and Mr. Keiper gave their assurances that they fully understood the nature and extent of their prospective duties, and would abide by them. In addition, they agreed and confirmed that:

> (a) Mr. Woollcombe would no longer be an advisor to Clearwater and Equilibrium with respect to Stelco;
> (b) Clearwater and Equilibrium would no longer be represented by counsel in the

CCAA proceedings; and

(c) Clearwater and Equilibrium then had no involvement in, and would have no future involvement, in any bid for Stelco.

[21] On the basis of the foregoing -- and satisfied "that Messrs. Keiper and Woollcombe would make a positive contribution to the various issues before the Board both in [the] restructuring and the ongoing operation of the business" -- the Board made the appointments on February 18, 2005.

[22] Seven days later, the motion judge found it "appropriate, just, necessary and reasonable to declare" those appointments "to be of no force and effect" and to remove Messrs. Woollcombe and Keiper from the Board. He did so not on the basis of any actual conduct on the part of the appellants as directors of Stelco but [page14] because there was some risk of anticipated conduct in the future. The gist of the motion judge's rationale is found in the following passage from his reasons (at para. 23):

> In these particular circumstances and aside from the Board feeling coerced into the appointments for the sake of continuing stability, I am not of the view that it would be appropriate to wait and see if there was any explicit action on behalf of K and W while conducting themselves as Board members which would demonstrate that they had not lived up to their obligations to be "neutral". They may well conduct themselves beyond reproach. But if they did not, the fallout would be very detrimental to Stelco and its ability to successfully emerge. What would happen to the bids in such a dogfight? I fear that it would be trying to put Humpty Dumpty back together again. The same situation would prevail even if K and W conducted themselves beyond reproach but with the Board continuing to be concerned that they not do anything seemingly offensive to the bloc. The risk to the process and to Stelco in its emergence is simply too great to risk the wait and see approach.

Part III -- Leave to Appeal

[23] Because of the "real time" dynamic of this restructuring project, Laskin J.A. granted an order on March 4, 2005, expediting the appellants' motion for leave to appeal, directing that it be heard orally and, if leave be granted, directing that the appeal be heard at the same time. The leave motion and the appeal were argued together, by order of the panel, on March 18, 2005.

[24] This court has said that it will only sparingly grant leave to appeal in the context of a CCAA proceeding and will only do so where there are "serious and arguable grounds that are of real and significant interest to the parties": Country Style Food Services Inc. (Re), [2002] O.J. No. 1377, 158 O.A.C. 30 (C.A.), at para. 15. This criterion is determined in accordance with a four-pronged test, namely,

(a) whether the point on appeal is of significance to the practice;
(b) whether the point is of significance to the action;

(c) whether the appeal is prima facie meritorious or frivolous;
(d) whether the appeal will unduly hinder the progress of the action.

[25] Counsel agree that (d) above is not relevant to this proceeding, given the expedited nature of the hearing. In my view, the tests set out in (a) - (c) are met in the circumstances, and as such, leave should be granted. The issue of the court's jurisdiction to intervene in corporate governance issues during a CCAA restructuring, and the scope of its discretion in doing so, are questions of considerable importance to the practice and on [page15] which there is little appellate jurisprudence. While Messrs. Woollcombe and Keiper are pursuing their remedies in their own right, and the company and its directors did not take an active role in the proceedings in this court, the Board and the company did stand by their decision to appoint the new directors at the hearing before the motion judge and in this court, and the question of who is to be involved in the Board's decision-making process continues to be of importance to the CCAA proceedings. From the reasons that follow it will be e vident that in my view the appeal has merit.

[26] Leave to appeal is therefore granted.

Part IV -- The Appeal

The Positions of the Parties

[27] The appellants submit that,

(a) in exercising its discretion under the CCAA, the court is not exercising its "inherent jurisdiction" as a superior court;
(b) there is no jurisdiction under the CCAA to remove duly elected or appointed directors, notwithstanding the broad discretion provided by s. 11 of that Act; and that,
(c) even if there is jurisdiction, the motion judge erred:

(i) by relying upon the administrative law test for reasonable apprehension of bias in determining that the directors should be removed;
(ii) by rejecting the application of the "business judgment" rule to the unanimous decision of the Board to appoint two new directors; and,
(iii) by concluding that Clearwater and Equilibrium, the shareholders with whom the appellants are associated, were focussed solely on a short-term investment horizon, without any evidence to that effect, and therefore concluding that there was a tangible risk that the appellants would not be neutral and act in the best interests of Stelco and all stakeholders in carrying out their duties as directors.

[28] The respondents' arguments are rooted in fairness and process. They say, first, that the appointment of the appellants as directors has poisoned the atmosphere of the CCAA proceedings and, second, that it threatens to undermine the even-handedness and integrity of the capital raising process, thus jeopardizing the [page16] ability of the court at the end of the day to approve any compromise or arrangement emerging from that process. The respondents contend that Farley J. had jurisdiction to ensure the integrity of the CCAA process, including the capital raising process Stelco had asked him to approve, and that this court should not interfere with his decision that it was necessary to remove Messrs. Woollcombe and Keiper from the Board in order to ensure the integrity of that process. A judge exercising a supervisory function during a CCAA proceeding is owed considerable deference: Re Algoma Steel Inc., [2001] O.J. No. 1943, 25 C.B.R. (4th) 194 (C.A.), at para. 8.

[29] The crux of the respondents' concern is well-articulated in the following excerpt from para. 72 of the factum of the Retired Salaried Beneficiaries:

> The appointments of Keiper and Woollcombe violated every tenet of fairness in the restructuring process that is supposed to lead to a plan of arrangement. One stakeholder group -- particular investment funds that have acquired Stelco shares during the CCAA itself -- have been provided with privileged access to the capital raising process, and voting seats on the Corporation's Board of Directors and Restructuring Committee. No other stakeholder has been treated in remotely the same way. To the contrary, the salaried retirees have been completely excluded from the capital raising process and have no say whatsoever in the Corporation's decision-making process.

[30] The respondents submit that fairness, and the perception of fairness, underpin the CCAA process, and depend upon effective judicial supervision: see Re Olympia & York Development Ltd. (1993), 12 O.R. (3d) 500, [1993] O.J. No. 545 (Gen. Div.); Re Ivaco Inc., [2004] O.J. No. 2483, 3 C.B.R. (5th) 33 (S.C.J.), at paras. 15-16. The motion judge reasonably decided to remove the appellants as directors in the circumstances, they say, and this court should not interfere.

Jurisdiction

[31] The motion judge concluded that he had the power to rescind the appointments of the two directors on the basis of his "inherent jurisdiction" and "the discretion given to the court pursuant to the CCAA". He was not asked to, nor did he attempt to rest his jurisdiction on other statutory powers imported into the CCAA.

[32] The CCAA is remedial legislation and is to be given a liberal interpretation to facilitate its objectives: Babcock & Wilcox Canada Ltd. (Re), [2000] O.J. No. 786, 5 B.L.R. (3d) 75 (S.C.J.), at para. 11. See also, Chef Ready Foods Ltd. v. Hong Kong Bank of Canada, [1990] B.C.J. No. 2384, 4 C.B.R. (3d) 311 (C.A.), at p. 320 C.B.R.; Re Lehndorff General Partners Ltd., [1993] O.J. No. 14, 17 C.B.R. (3d) 24 (Gen. Div.). [page17]Courts have adopted this approach in the past to rely on inherent jurisdiction, or alternatively on the broad jurisdiction under s. 11 of the CCAA, as the

source of judicial power in a CCAA proceeding to "fill in the gaps" or to "put flesh on the bones" of that Act: see Re Dylex Ltd., [1995] O.J. No. 595, 31 C.B.R. (3d) 106 (Gen. Div. (Commercial List)), Royal Oak Mines Inc. (Re), [1999] O.J. No. 864, 7 C.B.R. (4th) 293 (Gen. Div. (Commercial List); and Westar Mining Ltd. (Re), [1992] B.C.J. No. 1360, 70 B.C.L.R. (2d) 6 (S.C.).

[33] It is not necessary, for purposes of this appeal, to determine whether inherent jurisdiction is excluded for all supervisory purposes under the CCAA, by reason of the existence of the statutory discretionary regime provided in that Act. In my opinion, however, the better view is that in carrying out his or her supervisory functions under the legislation, the judge is not exercising inherent jurisdiction but rather the statutory discretion provided by s. 11 of the CCAA and supplemented by other statutory powers that may be imported into the exercise of the s. 11 discretion from other statutes through s. 20 of the CCAA.

Inherent jurisdiction

[34] Inherent jurisdiction is a power derived "from the very nature of the court as a superior court of law", permitting the court "to maintain its authority and to prevent its process being obstructed and abused". It embodies the authority of the judiciary to control its own process and the lawyers and other officials connected with the court and its process, in order "to uphold, to protect and to fulfill the judicial function of administering justice according to law in a regular, orderly and effective manner". See I.H. Jacob, "The Inherent Jurisdiction of the Court" (1970) 23 Current Legal Problems 27-28. In Halsbury's Laws of England, 4th ed. (London: LexisNexis UK, 1973 --), vol. 37, at para. 14, the concept is described as follows:

> In sum, it may be said that the inherent jurisdiction of the court is a virile and viable doctrine, and has been defined as being the reserve or fund of powers, a residual source of powers, which the court may draw upon as necessary whenever it is just or equitable to do so, in particularly to ensure the observation of the due process of law, to prevent improper vexation or oppression, to do justice between the parties and to secure a fair trial between them.

[35] In spite of the expansive nature of this power, inherent jurisdiction does not operate where Parliament or the legislature has acted. As Farley J. noted in Royal Oak Mines, supra, inherent jurisdiction is "not limitless; if the legislative body has not left a functional gap or vacuum, then inherent jurisdiction should [page18] not be brought into play" (para. 4). See also, Baxter Student Housing Ltd. v. College Housing Co-operative Ltd., [1976] 2 S.C.R. 475, 57 D.L.R. (3d) 1, at p. 480 S.C.R.; Richtree Inc. (Re) (2005), 74 O.R. (3d) 174, [2005] O.J. No. 251 (S.C.J.).

[36] In the CCAA context, Parliament has provided a statutory framework to extend protection to a company while it holds its creditors at bay and attempts to negotiate a compromised plan of arrangement that will enable it to emerge and continue as a viable economic entity, thus benefiting society and the company in the long run, along with the company's creditors, shareholders, employees and other stakeholders. The s. 11 discretion is the engine that drives this broad and

flexible statutory scheme, and that for the most part supplants the need to resort to inherent jurisdiction. In that regard, I agree with the comment of Newbury J.A. in Clear Creek Contracting Ltd. v. Skeena Cellulose Inc., [2003] B.C.J. No. 1335, 43 C.B.R. (4th) 187 (C.A.), at para. 46, that:

> ... the court is not exercising a power that arises from its nature as a superior court of law, but is exercising the discretion given to it by the CCAA. ... This is the discretion, given by s. 11, to stay proceedings against the debtor corporation and the discretion, given by s. 6, to approve a plan which appears to be reasonable and fair, to be in accord with the requirements and objects of the statute, and to make possible the continuation of the corporation as a viable entity. It is these considerations the courts have been concerned with in the cases discussed above[2] at the end of the docuemnt], rather than the integrity of their own process.

[37] As Jacob observes, in his article "The Inherent Jurisdiction of the Court", supra, at p. 25:

> The inherent jurisdiction of the court is a concept which must be distinguished from the exercise of judicial discretion. These two concepts resemble each other, particularly in their operation, and they often appear to overlap, and are therefore sometimes confused the one with the other. There is nevertheless a vital juridical distinction between jurisdiction and discretion, which must always be observed.

[38] I do not mean to suggest that inherent jurisdiction can never apply in a CCAA context. The court retains the ability to control its own process, should the need arise. There is a distinction, however -- difficult as it may be to draw -- between the court's process with respect to the restructuring, on the one hand, and the course of action involving the negotiations and corporate actions accompanying them, which are the company's process, on the other hand. The court simply supervises the latter [page19]process through its ability to stay, restrain or prohibit proceedings against the company during the plan negotiation period "on such terms as it may impose"[3] at the end fo the document]. Hence the better view is that a judge is generally exercising the court's statutory discretion under s. 11 of the Act when supervising a CCAA proceeding. The order in this case could not be founded on inherent jurisdiction because it is designed to supervise the company's process, not the court's process.

The section 11 discretion

[39] This appeal involves the scope of a supervisory judge's discretion under s. 11 of the CCAA, in the context of corporate governance decisions made during the course of the plan negotiating and approval process and, in particular, whether that discretion extends to the removal of directors in that environment. In my view, the s. 11 discretion -- in spite of its considerable breadth and flexibility -- does not permit the exercise of such a power in and of itself. There may be situations where a judge in a CCAA proceeding would be justified in ordering the removal of directors pursuant to the oppression remedy provisions found in s. 241 of the Canada Business Corporation Act, R.S.C. 1985, c. C-44 ("CBCA"), and imported into the exercise of the s. 11 discretion through

s. 20 of the CCAA. However, this was not argued in the present case, and the facts before the court would not justify the removal of Messrs. Woollcombe and Keiper on oppression remedy gr ounds.

[40] The pertinent portions of s. 11 of the CCAA provide as follows:

> Powers of court
>
> 11(1) Notwithstanding anything in the Bankruptcy and Insolvency Act or the Winding-up Act, where an application is made under this Act in respect of a company, the court, on the application of any person interested in the matter, may, subject to this Act, on notice to any other person or without notice as it may see fit, make an order under this section.
>
> . . . . .
>
> Initial application court orders
>
> (3) A court may, on an initial application in respect of a company, make an order on such terms as it may impose, effective for such period as the court deems necessary not exceeding thirty days.
>
> (a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1); [page20]
> (b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
> (c) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.
>
> Other than initial application court orders
>
> (4) A court may, on an application in respect of a company other than an initial application, make an order on such terms as it may impose,
>
> (a) staying, until otherwise ordered by the court, for such period as the court deems necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

. . . . .

Burden of proof on application

(6) The court shall not make an order under subsection (3) or (4) unless

(a) the applicant satisfies the court that circumstances exist that make such an order appropriate; and

(b) in the case of an order under subsection (4), the applicant also satisfied the court that the applicant has acted, and is acting, in good faith and with due diligence.

[41] The rule of statutory interpretation that has now been accepted by the Supreme Court of Canada, in such cases as R. v. Sharpe, [2001] 1 S.C.R. 45, [2001] S.C.J. No. 3, at para. 33, and Rizzo & Rizzo Shoes Ltd. (Re), [1998] 1 S.C.R. 27, [1998] S.C.J. No. 2, at para. 21, is articulated in E.A. Driedger, The Construction of Statutes, 2nd ed. (Toronto: Butterworths, 1983) as follows:

> Today, there is only one principle or approach, namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

See also Ruth Sullivan, Sullivan and Driedger on the Construction of Statutes, 4th ed. (Toronto: Butterworths, 2002), at p. 262.

[42] The interpretation of s. 11 advanced above is true to these principles. It is consistent with the purpose and scheme of the CCAA, as articulated in para. 38 above, and with the fact that corporate governance matters are dealt with in other statutes. In addition, it honours the historical reluctance of courts to intervene in such matters, or to second-guess the business decisions [page21]made by directors and officers in the course of managing the business and affairs of the corporation.

[43] Mr. Leon and Mr. Swan argue that matters relating to the removal of directors do not fall within the court's discretion under s. 11 because they fall outside of the parameters of the court's role in the restructuring process, in contrast to the company's role in the restructuring process. The court's role is defined by the "on such terms as may be imposed" jurisdiction under subparas. 11(3)(a) -- (c) and 11(4)(a) -- (c) of the CCAA to stay, or restrain, or prohibit proceedings against the company during the "breathing space" period for negotiations and a plan. I agree.

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

[45] With these principles in mind, I turn to an analysis of the various factors underlying the interpretation of the s. 11 discretion.

[46] I start with the proposition that at common law directors could not be removed from office during the term for which they were elected or appointed: London Finance Corp. Ltd. v. Banking Service Corp. Ltd., [1922] O.J. No. 378, 23 O.W.N. 138 (H.C.); Stephenson v. Vokes, [1896] O.J. No. 191, 27 O.R. 691 (H.C.J.). The authority to remove must therefore be found in statute law.

[47] In Canada, the CBCA and its provincial equivalents govern the election, appointment and removal of directors, as well as providing for their duties and responsibilities. Shareholders elect directors, but the directors may fill vacancies that occur on the board of directors pending a further shareholders meeting: [page22] CBCA, ss. 106(3) and 111[4] at the end of the document]. The specific power to remove directors is vested in the shareholders by s. 109(1) of the CBCA. However, s. 241 empowers the court -- where it finds that oppression as therein defined exists -- to "make any interim or final order it thinks fit", including (s. 241(3)(e)) "an order appointing directors in place of or in addition to all or any of the directors then in office". This power has been utilized to remove directors, but in very rare cases, and only in circumstances where there has been actual conduct rising to the level of misconduct required to trigger oppression remedy relief: see, for example, Catalyst Fund General Partner I Inc. v. Hollinger Inc., [2004] O.J. No. 4722, 1 B.L.R. (4th) 186 (S.C.J.).

[48] There is therefore a statutory scheme under the CBCA (and similar provincial corporate legislation) providing for the election, appointment and removal of directors. Where another applicable statute confers jurisdiction with respect to a matter, a broad and undefined discretion provided in one statute cannot be used to supplant or override the other applicable statute. There is no legislative "gap" to fill. See Baxter Student Housing Ltd. v. College Housing Cooperative Ltd., supra, at p. 480 S.C.R.; Royal Oak Mines Inc. (Re), supra; and Richtree Inc. (Re), supra.

[49] At para. 7 of his reasons, the motion judge said:

> The board is charged with the standard duty of "manage[ing], [sic] or supervising the management, of the business and affairs of the corporation": s. 102(1) CBCA. Ordinarily the Court will not interfere with the composition of the board of directors. However, if there is good and sufficient valid reason to do so, then the Court must not hesitate to do so to correct a problem. The directors should not be required to constantly look over their shoulders for this would be the sure recipe for board paralysis which would be so detrimental to a restructuring process; thus interested parties should only initiate a motion where it is reasonably obvious that there is a problem, actual or poised to become actual.

(Emphasis added)

[50] Respectfully, I see no authority in s. 11 of the CCAA for the court to interfere with the composition of a board of directors on such a basis.

[51] Court removal of directors is an exceptional remedy, and one that is rarely exercised in corporate law. This reluctance is rooted in the historical unwillingness of courts to interfere with the internal management of corporate affairs and in the court's well-established deference to decisions made by directors and officers in [page23] the exercise of their business judgment when managing the business and affairs of the corporation. These factors also bolster the view that where the CCAA is silent on the issue, the court should not read into the s. 11 discretion an extraordinary power -- which the courts are disinclined to exercise in any event -- except to the extent that that power may be introduced through the application of other legislation, and on the same principles that apply to the application of the provisions of the other legislation.

The oppression remedy gateway

[52] The fact that s. 11 does not itself provide the authority for a CCAA judge to order the removal of directors does not mean that the supervising judge is powerless to make such an order, however. Section 20 of the CCAA offers a gateway to the oppression remedy and other provisions of the CBCA and similar provincial statutes. Section 20 states:

> 20. The provisions of this Act may be applied together with the provisions of any Act of Parliament or of the legislature of any province that authorizes or makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them.

[53] The CBCA is legislation that "makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them". Accordingly, the powers of a judge under s. 11 of the CCAA may be applied together with the provisions of the

CBCA, including the oppression remedy provisions of that statute. I do not read s. 20 as limiting the application of outside legislation to the provisions of such legislation dealing specifically with the sanctioning of compromises and arrangements between the company and its shareholders. The grammatical structure of s. 20 mandates a broader interpretation and the oppression remedy is, therefore, available to a supervising judge in appropriate circumstances.

[54] I do not accept the respondents' argument that the motion judge had the authority to order the removal of the appellants by virtue of the power contained in s. 145(2)(b) of the CBCA to make an order "declaring the result of the disputed election or appointment" of directors. In my view, s. 145 relates to the procedures underlying disputed elections or appointments, and not to disputes over the composition of the board of directors itself. Here, it is conceded that the appointment of Messrs. Woollcombe and Keiper as directors complied with all relevant statutory requirements. Farley J. quite properly did not seek to base his jurisdiction on any such authority. [page24]

The level of conduct required

[55] Colin Campbell J. recently invoked the oppression remedy to remove directors, without appointing anyone in their place, in Catalyst Fund General Partner I Inc. v. Hollinger Inc., supra. The bar is high. In reviewing the applicable law, C. Campbell J. said (para. 68):

> Director removal is an extraordinary remedy and certainly should be imposed most sparingly. As a starting point, I accept the basic proposition set out in Peterson, "Shareholder Remedies in Canada".[5] at the end of the document]
>
> > SS. 18.172 Removing and appointing directors to the board is an extreme form of judicial intervention. The board of directors is elected by the shareholders, vested with the power to manage the corporation, and appoints the officers of the company who undertake to conduct the day-to-day affairs of the corporation. [Footnote omitted.] It is clear that the board of directors has control over policymaking and management of the corporation. By tampering with a board, a court directly affects the management of the corporation. If a reasonable balance between protection of corporate stakeholders and the freedom of management to conduct the affairs of the business in an efficient manner is desired, altering the board of directors should be a measure of last resort. The order could be suitable where the continuing presence of the incumbent directors is harmful to both the company and the interests of corporate stakeholders, and where the appointment of a new director or directors would remedy the oppressive conduct without a receiver or receiver-manager.

(Emphasis added)

[56] C. Campbell J. found that the continued involvement of the Ravelston directors in the

Hollinger situation would "significantly impede" the interests of the public shareholders and that those directors were "motivated by putting their interests first, not those of the company" (paras. 82-83). The evidence in this case is far from reaching any such benchmark, however, and the record would not support a finding of oppression, even if one had been sought.

[57] Everyone accepts that there is no evidence the appellants have conducted themselves, as directors -- in which capacity they participated over two days in the bid consideration exercise -- in anything but a neutral fashion, having regard to the best interests of Stelco and all of the stakeholders. The motion judge acknowledged that the appellants "may well conduct themselves beyond reproach". However, he simply decided there was a risk -- a reasonable apprehension -- that Messrs. Woollcombe and Keiper would not live up to their obligations to be neutral in the future. [page25]

[58] The risk or apprehension appears to have been founded essentially on three things: (1) the earlier public statements made by Mr. Keiper about "maximizing shareholder value"; (2) the conduct of Clearwater and Equilibrium in criticizing and opposing the Stalking Horse Bid; and (3) the motion judge's opinion that Clearwater and Equilibrium -- the shareholders represented by the appellants on the Board -- had a "vision" that "usually does not encompass any significant concern for the long-term competitiveness and viability of an emerging corporation", as a result of which the appellants would approach their directors' duties looking to liquidate their shares on the basis of a "short-term hold" rather than with the best interests of Stelco in mind. The motion judge transposed these concerns into anticipated predisposed conduct on the part of the appellants as directors, despite their apparent understanding of their duties as directors and their assurances that they would act in the best interests of Stelco. He therefore concluded that "the risk to the process and to Stelco in its emergence [was] simply too great to risk the wait and see approach".

[59] Directors have obligations under s. 122(1) of the CBCA (a) to act honestly and in good faith with a view to the best interest of the corporation (the "statutory fiduciary duty" obligation), and (b) to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances (the "duty of care" obligation). They are also subject to control under the oppression remedy provisions of s. 241. The general nature of these duties does not change when the company approaches, or finds itself in, insolvency: Peoples Department Stores Inc. (Trustee of) v. Wise, [2004] 3 S.C.R. 461, [2004] S.C.J. No. 64, at paras. 42-49.

[60] In Peoples the Supreme Court noted that "the interests of the corporation are not to be confused with the interests of the creditors or those of any other stakeholders" (para. 43), but also accepted "as an accurate statement of the law that in determining whether [directors] are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, inter alia, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment" (para. 42). Importantly as well -- in the context of "the shifting interest and incentives of shareholders and creditors" -- the court stated (para. 47):

> In resolving these competing interests, it is incumbent upon the directors to act honestly and in good faith with a view to the best interests of the corporation. In using their skills for the benefit of the corporation when it is in troubled waters financially, the directors must be careful to attempt to act in [page26]its best interests by creating a "better" corporation, and not to favour the interests of any one group of stakeholders.

[61] In determining whether directors have fallen foul of those obligations, however, more than some risk of anticipated misconduct is required before the court can impose the extraordinary remedy of removing a director from his or her duly elected or appointed office. Although the motion judge concluded that there was a risk of harm to the Stelco process if Messrs. Woollcombe and Keiper remained as directors, he did not assess the level of that risk. The record does not support a finding that there was a sufficient risk of sufficient misconduct to warrant a conclusion of oppression. The motion judge was not asked to make such a finding, and he did not do so.

[62] The respondents argue that this court should not interfere with the decision of the motion judge on grounds of deference. They point out that the motion judge has been case-managing the restructuring of Stelco under the CCAA for over 14 months and is intimately familiar with the circumstances of Stelco as it seeks to restructure itself and emerge from court protection.

[63] There is no question that the decisions of judges acting in a supervisory role under the CCAA, and particularly those of experienced commercial list judges, are entitled to great deference: see Algoma Steel Inc. v. Union Gas Ltd. (2003), 63 O.R. (3d) 78, [2003] O.J. No. 71 (C.A.), at para. 16. The discretion must be exercised judicially and in accordance with the principles governing its operation. Here, respectfully, the motion judge misconstrued his authority, and made an order that he was not empowered to make in the circumstances.

[64] The appellants argued that the motion judge made a number of findings without any evidence to support them. Given my decision with respect to jurisdiction, it is not necessary for me to address that issue.

The business judgment rule

[65] The appellants argue as well that the motion judge erred in failing to defer to the unanimous decision of the Stelco directors in deciding to appoint them to the Stelco Board. It is well-established that judges supervising restructuring proceedings -- and courts in general -- will be very hesitant to second-guess the business decisions of directors and management. As the Supreme Court of Canada said in Peoples, supra, at para. 67:

> Courts are ill-suited and should be reluctant to second-guess the application of business expertise to the considerations that are involved in corporate decision making ... [page27]

[66] In Brant Investments Ltd. v. KeepRite Inc. (1991), 3 O.R. (3d) 289, [1991] O.J. No. 683

(C.A.), at p. 320 O.R., this court adopted the following statement by the trial judge, Anderson J.:

> Business decisions, honestly made, should not be subjected to microscopic examination. There should be no interference simply because a decision is unpopular with the minority.[6] at the end of the document]
>
> [67] McKinlay J.A. then went on to say [at p. 320 O.R.]:
>
> There can be no doubt that on an application under s. 234[7] at the end of the document] the trial judge is required to consider the nature of the impugned acts and the method in which they were carried out. That does not meant that the trial judge should substitute his own business judgment for that of managers, directors, or a committee such as the one involved in assessing this transaction. Indeed, it would generally be impossible for him to do so, regardless of the amount of evidence before him. He is dealing with the matter at a different time and place; it is unlikely that he will have the background knowledge and expertise of the individuals involved; he could have little or no knowledge of the background and skills of the persons who would be carrying out any proposed plan; and it is unlikely that he would have any knowledge of the specialized market in which the corporation operated. In short, he does not know enough to make the business decision required.

[68] Although a judge supervising a CCAA proceeding develops a certain "feel" for the corporate dynamics and a certain sense of direction for the restructuring, this caution is worth keeping in mind. See also Clear Creek Contracting Ltd. v. Skeena Cellulose Inc., supra; Sammi Atlas Inc. (Re), [1998] O.J. No. 1089, 3 C.B.R. (4th) 171 (Gen. Div.); Olympia & York Developments Ltd. (Re), supra; Re Alberta Pacific Terminals Ltd., [1991] B.C.J. No. 1065, 8 C.B.R. (4th) 99 (S.C.). The court is not catapulted into the shoes of the board of directors, or into the seat of the chair of the board, when acting in its supervisory role in the restructuring.

[69] Here, the motion judge was alive to the "business judgment" dimension in the situation he faced. He distinguished the application of the rule from the circumstances, however, stating at para. 18 of his reasons:

> With respect I do not see the present situation as involving the "management of the business and affairs of the corporation", but rather as a quasi-constitutional aspect of the corporation entrusted albeit to the Board pursuant to s. 111(1) of the CBCA. I agree that where a board is actually engaged in the business of a judgment situation, the board should be given appropriate deference. However, to the contrary in this situation, I do not see it as a [page28]situation calling for (as asserted) more deference, but rather considerably less than that. With regard to this decision of the Board having impact upon the capital raising process, as I conclude it would, then similarly deference ought

not to be given.

[70] I do not see the distinction between the directors' role in "the management of the business and affairs of the corporation" (CBCA, s. 102) -- which describes the directors' overall responsibilities -- and their role with respect to a "quasi-constitutional aspect of the corporation" (i.e., in filling out the composition of the board of directors in the event of a vacancy). The "affairs" of the corporation are defined in s. 2 of the CBCA as meaning "the relationships among a corporation, its affiliates and the shareholders, directors and officers of such bodies corporate but does not include the business carried on by such bodies corporate". Corporate governance decisions relate directly to such relationships and are at the heart of the Board's business decision-making role regarding the corporation's business and affairs. The dynamics of such decisions, and the intricate balancing of competing interests and other corporate-related factors that goes into making them, are no more within the purview of the court's knowledge and expertise than other business decisions, and they deserve the same deferential approach. Respectfully, the motion judge erred in declining to give effect to the business judgment rule in the circumstances of this case.

[71] This is not to say that the conduct of the Board in appointing the appellants as directors may never come under review by the supervising judge. The court must ultimately approve and sanction the plan of compromise or arrangement as finally negotiated and accepted by the company and its creditors and stakeholders. The plan must be found to be fair and reasonable before it can be sanctioned. If the Board's decision to appoint the appellants has somehow so tainted the capital raising process that those criteria are not met, any eventual plan that is put forward will fail.

[72] The respondents submit that it makes no sense for the court to have jurisdiction to declare the process flawed only after the process has run its course. Such an approach to the restructuring process would be inefficient and a waste of resources. While there is some merit in this argument, the court cannot grant itself jurisdiction where it does not exist. Moreover, there are a plethora of checks and balances in the negotiating process itself that moderate the risk of the process becoming irretrievably tainted in this fashion -- not the least of which is the restraining effect of the prospect of such a consequence. I do not think that this argument can prevail. In addition, the court at all times retains its broad and [page29] flexible supervisory jurisdiction -- a jurisdiction which feeds the creativity that makes the CCAA work so well -- in order to address fairness and process concerns along the way. This case relates only to the court's exceptional power to order the removal of di rectors.

The reasonable apprehension of bias analogy

[73] In exercising what he saw as his discretion to remove the appellants as directors, the motion judge thought it would be useful to "borrow the concept of reasonable apprehension of bias ... with suitable adjustments for the nature of the decision making involved" (para. 8). He stressed that "there was absolutely no allegation against [Mr. Woollcombe and Mr. Keiper] of any actual aebias' or its equivalent" (para. 8). He acknowledged that neither was alleged to have done anything wrong

since their appointments as directors, and that at the time of their appointments the appellants had confirmed to the Board that they understood and would abide by their duties and responsibilities as directors, including the responsibility to act in the best interests of the corporation and not in their own interests as shareholders. In the end, however, he concluded that because of their prior public statements that they intended to "pursue efforts to maximize shareholder value at Stelco", and because of the nature of their business and the way in which they had been accumulating their shareholding position during the restructuring, and because of their linkage to 40 per cent of the common shareholders, there was a risk that the appellants would not conduct themselves in a neutral fashion in the best interests of the corporation as directors.

[74] In my view, the administrative law notion of apprehension of bias is foreign to the principles that govern the election, appointment and removal of directors, and to corporate governance considerations in general. Apprehension of bias is a concept that ordinarily applies to those who preside over judicial or quasi-judicial decision-making bodies, such as courts, administrative tribunals or arbitration boards. Its application is inapposite in the business decision-making context of corporate law. There is nothing in the CBCA or other corporate legislation that envisages the screening of directors in advance for their ability to act neutrally, in the best interests of the corporation, as a prerequisite for appointment.

[75] Instead, the conduct of directors is governed by their common law and statutory obligations to act honestly and in good faith with a view to the best interests of the corporation, and to exercise the care, diligence and skill that a reasonably [page30]prudent person would exercise in comparable circumstances (CBCA, s. 122(1)(a) and (b)). The directors also have fiduciary obligations to the corporation, and they are liable to oppression remedy proceedings in appropriate circumstances. These remedies are available to aggrieved complainants -- including the respondents in this case -- but they depend for their applicability on the director having engaged in conduct justifying the imposition of a remedy.

[76] If the respondents are correct, and reasonable apprehension that directors may not act neutrally because they are aligned with a particular group of shareholders or stakeholders is sufficient for removal, all nominee directors in Canadian corporations, and all management directors, would automatically be disqualified from serving. No one suggests this should be the case. Moreover, as Iacobucci J. noted in Blair v. Consolidated Enfield Corp., [1995] 4 S.C.R. 5, [1995] S.C.J. No. 29, at para. 35, "persons are assumed to act in good faith unless proven otherwise". With respect, the motion judge approached the circumstances before him from exactly the opposite direction. It is commonplace in corporate/commercial affairs that there are connections between directors and various stakeholders and that conflicts will exist from time to time. Even where there are conflicts of interest, however, directors are not removed from the board of directors; they are simply obliged to disclose the conflict and, in appropriate cases, to abstain from voting. The issue to be determined is not whether there is a connection between a director and other shareholders or stakeholders, but rather whether there has been some conduct on the part of the director that will justify the imposition of a corrective sanction. An apprehension of bias approach

does not fit this sort of analysis.

Part V -- Disposition

[77] For the foregoing reasons, then, I am satisfied that the motion judge erred in declaring the appointment of Messrs. Woollcombe and Keiper as directors of Stelco of no force and effect.

[78] I would grant leave to appeal, allow the appeal and set aside the order of Farley J. dated February 25, 2005.

[79] Counsel have agreed that there shall be no costs of the appeal.

Order accordingly.

[page31]

Notes

Note 1: R.S.C. 1985, c. C-36, as amended.

Note 2: The reference is to the decisions in Dyle, Royal Oak Mines and Westar, cited above.

Note 3: See para. 43, infra, where I elaborate on this decision.

Note 4: It is the latter authority that the directors of Stelco exercised when appointing the appellants to the Stelco Board.

Note 5: Dennis H. Peterson, Shareholder Remedies in Canada, looseleaf (Markham: LexisNexis -- Butterworths, 1989), at 18-47.

Note 6:Or, I would add, unpopular with other stakeholders.

Note 7: Now s. 241.

* * * * *

[* Editor's note: Schedule "A" was not attached to the copy received from the Court and therefore is not included in the judgment.]

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 VICTORIAN ORDER OF NURSES FOR CANADA

Court File No: CV-15-11192-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

Proceeding commenced at Toronto

BOOK OF AUTHORITIES OF THE APPLICANTS/ RESPONDENTS TO MOTION (RETURNABLE AUGUST 30, 2016)

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