

Court File No.: \_\_\_\_\_

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
(COMMERCIAL LIST)**

BETWEEN:

**KENSINGTON PRIVATE EQUITY FUND**

Applicant

- and -

**O2 INDUSTRIES INC.**

Respondent

**IN THE MATTER OF AN APPLICATION PURSUANT TO  
SECTION 243(1) OF THE *BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985,  
c. B-3, AS AMENDED; AND SECTION 101 OF THE *COURTS OF JUSTICE ACT*,  
R.S.O. 1990, c. C.43, AS AMENDED**

**FACTUM OF THE APPLICANT  
(Application Returnable May 27, 2021)**

**GOODMANS LLP**  
Barristers & Solicitors  
333 Bay Street, Suite 3400  
Toronto, ON M5H 2S7

**Bradley Wiffen** LSO#: 64279L  
bwiffen@goodmans.ca

**Trish Barrett** LSO#: 77904U  
tbarrett@goodmans.ca

Tel: 416.979.2211  
Fax: 416.979.1234

Lawyers for the Applicant

## **PART I - OVERVIEW**

1. This Application is made by Kensington Private Equity Fund (the “**Agent**”), on its own behalf and on behalf of the other Kensington Lenders (as defined below), for an Order (the “**Receivership Order**”) under subsection 243(1) of the *Bankruptcy and Insolvency Act* (Canada) (“**BIA**”) and section 101 of the *Courts of Justice Act* (Ontario) (“**CJA**”) appointing RSM Canada Limited (“**RSM**”) as receiver (in such capacity, the “**Receiver**”) of the assets, property and undertaking (the “**Property**”) of O2 Industries Inc. (the “**Debtor**”).<sup>1</sup>

2. The Agent is a secured creditor of the Debtor. The Debtor is indebted to the Kensington Lenders in the amount of approximately \$2,030,574.29 as of May 25, 2021, inclusive of accrued interest but exclusive of expenses, costs and other charges (the “**Indebtedness**”), pursuant to three convertible promissory notes issued by the Debtor to the Kensington Lenders (collectively, the “**Promissory Notes**”). As security for the obligations under the Promissory Notes, the Debtor granted to the Agent a security interest in its present and future assets, undertaking and property pursuant to a General Security Agreement dated March 31, 2021 (the “**General Security Agreement**”).

3. On May 14, 2021, the Agent demanded repayment of the Indebtedness and delivered to the Debtor a notice of intention to enforce security pursuant to subsection 244(1) of the BIA (the “**BIA Notice**”). The Debtor is insolvent and the Indebtedness remains outstanding. On May 18, 2021,

---

<sup>1</sup> Capitalized terms used but not defined herein have the meanings given to them in the Affidavit of Richard Nathan sworn May 25, 2021 (the “**Nathan Affidavit**”). Unless otherwise stated, all monetary amounts are expressed in United States dollars.

the Debtor delivered a written consent to the Agent's enforcement of its security, including the appointment of a Court-appointed receiver.

4. The Agent seeks the appointment of the Receiver in order to preserve the going concern value of the Debtor's business, obtain a stay of proceedings to prevent actions that could result in a further deterioration of the Debtor's financial condition, and provide a stabilized environment for the Receiver to conduct a sale process (the "**Sale Process**") to solicit interest in a value-maximizing transaction for the Debtor's business and property.

5. The Agent supports the immediate commencement of the Sale Process pursuant to the proposed sale procedures (the "**Sale Procedures**") developed in consultation with the proposed Receiver. Kensington, through a special purpose entity, has agreed to act as the stalking horse bidder in the sale process through a credit bid transaction for the acquisition of substantially all of the business and assets of the Debtor (the "**Stalking Horse Transaction**"). The Sale Procedures will enable the Receiver to test the market and ultimately proceed with the transaction that maximizes the value of the Debtor's business and assets.

6. The appointment of the Receiver is just and convenient in the circumstances, is permitted by the General Security Agreement, and is consented to by the Debtor. The appointment of the Receiver and the immediate commencement of the Sale Process are necessary having regard to the Debtor's financial condition. The Sale Process, supported by the Stalking Horse Transaction, is the best means in the circumstances to identify a value-maximizing transaction.

## **PART II- FACTS**

7. The relevant facts in connection with this Application are more fully set out in the affidavit of Richard Nathan sworn May 25, 2021 (the "**Nathan Affidavit**").

**A. Business of the Debtor and Financial Challenges**

8. The Debtor, which designs and manufactures personal respirators for consumer, healthcare, and military/law enforcement markets (the “**Business**”), is experiencing severe financial challenges. In 2020, the Debtor experienced a sudden increase in sales revenue as a result of demand for personal protective equipment (“**PPE**”) due to the COVID-19 pandemic. However, the PPE market has become saturated with excess supply and the Debtor’s sales revenues have declined precipitously to near pre-pandemic levels.

Nathan Affidavit at paras. 5, 41-42; Application Record, Tab 2.

9. During the brief period of heightened demand, the Debtor made substantial investments to expand its inventory and “scale up” its business operations on the assumption that peak pandemic-level demand for its products would persist for some time. It invested heavily in manufacturing and stockpiling inventory. As a result of a significant decline in demand, the Debtor currently has substantial inventories of its O2 Curve consumer respirator that it has been unable to sell through consumer or wholesale channels despite significantly discounting its price.

Nathan Affidavit at paras. 43-44; Application Record, Tab 2.

10. The Debtor’s financial position and cost structure are no longer sustainable. Despite the bridge financing advanced by the Kensington Lenders under the Promissory Notes, the Debtor has not been able to execute on its business plan by attracting new investors or generating cash flow through the sale of inventory. The Debtor is insolvent and the continuation of normal course business activity would cause the Debtor to exhaust its remaining liquidity in a matter of days.

Nathan Affidavit at paras. 5, 43, 53-54 and 62; Application Record, Tab 2.

**B. The Debtor's Indebtedness to the Kensington Lenders**

11. The Debtor is directly indebted to the Agent pursuant to the Promissory Notes issued by the Debtor to the Agent, as lender and agent on behalf of Kensington Venture Fund II, L.P. (“**KVFII**”) and Kensington (Parallel) Venture Fund II, L.P. (“**KVFII Parallel**”) and, together with the Agent and KVFII, the “**Kensington Lenders**”).

Nathan Affidavit at para. 27; Application Record, Tab 2.

12. The Kensington Lenders advanced funding to the Debtor under the Promissory Notes on March 31, 2021, April 13, 2021 and May 10, 2021 in an effort to stabilize the Debtor's business while it pursued various restructuring initiatives. However, the Debtor's efforts to date have not resulted in a resolution of the many challenges facing the company and its liquidity has continued to deteriorate. Under the current circumstances, the Kensington Lenders are not prepared to provide further financing to the Debtor outside of a court-supervised process.

Nathan Affidavit at paras. 9, 27, 39, and 55; Application Record, Tab 2.

13. The insolvency of the Debtor and the material adverse change in its financial condition constitute events of default under the Promissory Notes, entitling the Agent to exercise its rights and remedies under the General Security Agreement. The Agent's enforcement rights include the right to appoint a receiver or institute court proceedings for the appointment of a receiver.

Nathan Affidavit at paras. 10, 56 and 58; Application Record, Tab 2.

14. The Debtor has consented to the immediate enforcement of the Agent's security, including the appointment of the Receiver.

Nathan Affidavit at paras. 12 and 61; Application Record, Tab 2.

### **PART III- ISSUES**

15. The issues to be considered by this Court are:

- (a) whether it is just and convenient at the present time for this Court to appoint the Receiver; and
- (b) whether this Court should approve the Sale Procedures and the Stalking Horse Transaction for purposes of the Sale Process.

### **PART IV- LAW AND ARGUMENT**

#### **A. The Appointment of a Receiver is Just and Convenient**

16. Pursuant to subsection 243(1) and section 101 of the CJA, the Court may, on application of a secured creditor, appoint a receiver where it considers it “just or convenient” to do so.

BIA, s. 243(1); CJA, s. 101, Schedule B to this Factum.

17. In determining whether it is just and convenient to appoint a receiver, the Court “must have regard to all of the circumstances but in particular the nature of the property and the rights and interests of all parties in relation thereto, which includes the rights of the secured creditor and its security.” Typically, the issues for the Court to determine on a receivership application include the following:

- (a) the existence of a debt and default;
- (b) the quality of the security;
- (c) the need for the appointment of a receiver in view of alternate remedies available to the creditor;

- (d) the nature of the property;
- (e) the likelihood of maximizing the return to the parties;
- (f) the costs associated with the appointment; and
- (g) any need to preserve the property pending realization.

[RMB Australia Holdings Limited v. Seafeld Resources Ltd.](#), 2014 ONSC 5205 (Commercial List) at para. 28;

[Bank of Montreal v. Carnival National Leasing Limited and Carnival Automobiles Limited](#), 2011 ONSC 1007 (Commercial List) at paras. 24 and 27 [”*Carnival Leasing*”];

[Central 1 Credit Union v. UM Financial Inc. and UM Capital Inc.](#), 2011 ONSC 5612 (Commercial List) at para. 22.

18. The fact that a secured creditor has a right under its security documentation to appoint a receiver is of central importance. In cases where the security documentation provides for the appointment of a receiver, the analysis is focused on a consideration of whether it is in the interests of all concerned to have the receiver appointed by the court. As noted by Morawetz J, as he then was, in *Elleway*:

...while the appointment of a receiver is generally regarded as an extraordinary equitable remedy, courts do not regard the nature of the remedy as extraordinary or equitable where the relevant security document permits the appointment of a receiver. This is because the applicant is merely seeking to enforce a term of an agreement that was assented to by both parties.

[Elleway Acquisitions Ltd. v. Cruise Professionals Ltd.](#), 2013 ONSC 6866 (Commercial List) at para. 27.

19. It is not necessary for a creditor whose security documentation provides for the appointment of a receiver to demonstrate that it will suffer irreparable harm if the appointment of a receiver is not granted by the Court.

*Carnival Leasing*, *supra* at para. 28.

20. The appointment of the Receiver is just and convenient in the present circumstances, including for the following reasons:

- (a) the Debtor has been reliant on bridge financing from the Kensington Lenders to continue business operations. The Debtor has expended substantially all of the funding advanced under the Promissory Notes since March 31, 2021 and is now insolvent. The continuation of normal course business activity would cause the Debtor to exhaust its remaining liquidity in a matter of days;
- (b) events of default have occurred and are continuing under the Promissory Notes due to the insolvency of the Debtor and the material adverse change in its financial condition. As a result, the Indebtedness is immediately due and payable;
- (c) on May 14, 2021, the Agent demanded repayment of the Indebtedness and delivered the BIA Notice to the Debtor. The Indebtedness remains outstanding;
- (d) section 5.1(a)(iv)(A) of the General Security Agreement provides that the Agent may appoint a receiver or may institute proceedings in any court of competent jurisdiction for the appointment of a receiver;
- (e) on May 18, 2021, the Debtor provided its written consent to the immediate enforcement of the Agent's security, including the appointment of the Receiver;
- (f) the appointment of the Receiver is necessary to stabilize the Debtor's business and prevent further deterioration in its financial condition;



- (g) without access to additional financing in a court-supervised process, the Debtor will not have sufficient funding to continue business operations. A disorderly cessation of business activities would significantly impair the value of the business and the Agent's collateral; and
- (h) the receivership proceedings will provide a stabilized environment for the Receiver to conduct the Sale Process to solicit interest in and implement a sale transaction that maximizes the value of the Debtor's business and assets.

Nathan Affidavit at paras. 5, 7-10-11, 13, 39, 54, 56, 59, 61-62, 64 and 71;  
Application Record, Tab 2.

**B. The Sale Process and Stalking Horse Transaction Should Be Approved**

21. The proposed Receivership Order authorizes the Receiver to conduct the Sale Process in accordance with the Sale Procedures and approves the Stalking Horse Transaction as the stalking horse bid for purposes of the Sale Procedures.

22. While there is no statutory requirement for Court approval of a sale process, such approval is frequently sought in the context of BIA receiverships. In *CCM Master Qualified Fund Ltd. v. blutip Power Technologies Ltd.*, a receivership case involving a request to approve a sale process that included the use of a stalking horse credit bid, D.M. Brown J., as he then was, enunciated the following considerations with respect to the approval of a sale process:

Although the decision to approve a particular form of sales process is distinct from the approval of a proposed sale, the reasonableness and adequacy of any sales process proposed by a court-appointed receiver must be assessed in light of the factors which a court will take into account when considering the approval of a proposed sale. Those factors were identified by the Court of Appeal in its decision in *Royal Bank v. Soundair*: (i) whether the receiver has made a sufficient effort to get the best price and has not acted improvidently; (ii) the efficacy and integrity of the process by which offers are obtained; (iii) whether there has been

unfairness in the working out of the process; and, (iv) the interests of all parties.

Accordingly, when reviewing a sales and marketing process proposed by a receiver a court should assess:

- (i) the fairness, transparency and integrity of the proposed process;
- (ii) the commercial efficacy of the proposed process in light of the specific circumstances facing the receiver; and,
- (iii) whether the sales process will optimize the chances, in the particular circumstances, of securing the best possible price for the assets up for sale.

*CCM Master Qualified Fund Ltd. v. blutip Power Technologies Ltd.*, 2012 ONSC 1750 (Commercial List) at para. 6 [*“CCM”*].

23. The use of stalking horse bids, including credit bids, to set a baseline for the bidding process has been recognized by Canadian courts as a reasonable and useful element of a sales process. Stalking horse bids are beneficial where they ensure the continuation of a debtor’s business as a going concern while providing an opportunity for superior transactions to emerge. Stalking horse bids have been approved for use in receivership proceedings, BIA proposals and CCAA proceedings.

*CCM*, *supra* at para. 7;

*Graceway Canada Co., Re.*, 2011 ONSC 6403 (Commercial List) at para. 2;

*Mustang GP Ltd., Re.*, 2015 ONSC 6562 at para. 40.

24. In the *Danier Leather* BIA proposal proceedings, the Court approved a sale process supported by a stalking horse bid. Citing *CCM*, Penny J. noted that:

The use of a sale process that includes a stalking horse agreement maximizes value of business for the benefit of its stakeholders and enhances the fairness of the sale process. Stalking horse agreements are commonly used in insolvency proceedings to facilitate sales of businesses and assets and are intended to establish a baseline price and transactional structure for any superior bids from interested parties.

*Danier Leather Inc., Re.*, 2016 ONSC 1044 at para. 20.

25. The approval of the proposed Sale Procedures, supported by the Stalking Horse Transaction, is appropriate at this time for the following reasons:

- (a) the Debtor is facing severe liquidity issues and commencing the Sale Process without delay will reduce the cost of the receivership proceedings and enhance the prospects of completing a successful transaction;
- (b) the Sale Procedures are structured to enable the Receiver to solicit interest in and implement a sale transaction that maximizes the value of the Debtor's business and assets;
- (c) the Stalking Horse Transaction provides for the continuation of the Debtor's business as a going concern and therefore conveys a message of stability to customers, suppliers, employees and other stakeholders;
- (d) the Stalking Horse Transaction establishes a minimum value for the Debtor's business and provides for an auction process through which other higher-value transactions can emerge;
- (e) the Stalking Horse Transaction does not include any break fee in the event that a competing bid is chosen as the successful bid;
- (f) all bidders in the Sale Process will be provided with the form of purchase agreement for the Stalking Horse Transaction, thereby reducing the time and costs associated with the submission of competing bids in the Sale Process;

- (g) the Sale Procedures provide that the successful bid in the Sale Process, whether the Stalking Horse Transaction or a competing bid, is subject to approval by the Court on a subsequent motion; and
- (h) the Receiver supports the approval of the Sale Procedures and the approval of the Stalking Horse Transaction as the stalking horse bid pursuant to the proposed Receivership Order.

Nathan Affidavit at paras. 13-14, 26, 62, 64, 68, and 70-71; Application Record, Tab 2.

**PART V – CONCLUSION AND ORDER REQUESTED**

26. For the foregoing reasons, the Agent seeks the appointment of the Receiver and the granting of the Receivership Order in the form sought by the Agent.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED**

*Goodmans LLP*

---

GOODMANS LLP

May 25, 2021

**SCHEDULE A**  
**AUTHORITIES CITED**

1. *RMB Australia Holdings Limited v. Seafield Resources Ltd.*, 2014 ONSC 5205 (Commercial List)
2. *Bank of Montreal v. Carnival National Leasing Limited and Carnival Automobiles Limited*, 2011 ONSC 1007 (Commercial List)
3. *Central 1 Credit Union v. UM Financial Inc. and UM Capital Inc.*, 2011 ONSC 5612 (Commercial List)
4. *Elleway Acquisitions Ltd. v. Cruise Professionals Ltd.*, 2013 ONSC 6866 (Commercial List)
5. *CCM Master Qualified Fund Ltd. v. blutip Power Technologies Ltd.*, 2012 ONSC 1750 (Commercial List)
6. *Graceway Canada Co., Re.*, 2011 ONSC 6403 (Commercial List)
7. *Mustang GP Ltd., Re.*, 2015 ONSC 6562
8. *Danier Leather Inc., Re.*, 2016 ONSC 1044

## **SCHEDULE B**

### **STATUTES AND REGULATIONS**

#### ***BANKRUPTCY AND INSOLVENCY ACT*** **R.S.C., 1985, C. B-3, as amended**

##### **243(1)**

*Court may appoint receiver* – Subject to subsection (1.1), on application by a secured creditor, a court may appoint a receiver to do any or all of the following if it considers it to be just or convenient to do so:

- (a) take possession of all or substantially all of the inventory, accounts receivable or other property of an insolvent person or bankrupt that was acquired for or used in relation to a business carried on by the insolvent person or bankrupt;
- (b) exercise any control that the court considers advisable over that property and over the insolvent person's or bankrupt's business; or
- (c) take any other action that the court considers advisable.

#### ***COURTS OF JUSTICE ACT*** **R.S.O. 1990, c. C.43**

##### **101**

(1) In the Superior Court of Justice, an interlocutory injunction or mandatory order may be granted or a receiver or receiver and manager may be appointed by an interlocutory order, where it appears to a judge of the court to be just or convenient to do so.

(2) An order under subsection (1) may include such terms as are considered just.

Court File No.: \_\_\_\_\_

**IN THE MATTER OF AN APPLICATION PURSUANT TO SECTION 243(1) OF THE *BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985, c. B-3, AS AMENDED; AND SECTION 101 OF THE *COURTS OF JUSTICE ACT*, R.S.O. 1990, c. C.43, AS AMENDED**

**KENSINGTON PRIVATE**    - and -    **O2 INDUSTRIES INC.**  
**EQUITY FUND**  
Applicant                                  Respondent

---

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
(COMMERCIAL LIST)**

Proceedings commenced at Toronto

---

**FACTUM OF THE APPLICANT  
(Returnable May 27, 2021)**

---

**GOODMANS LLP**

Barristers & Solicitors  
333 Bay Street, Suite 3400  
Toronto, ON M5H 2S7

**Bradley Wiffen** LSO#: 64279L  
bwiffen@goodmans.ca

**Trish Barrett** LSO#: 77904U  
tbarrett@goodmans.ca

Tel: 416.979.2211  
Fax: 416.979.1234

Lawyers for the Applicant