

Tab C

2003 CarswellOnt 5296
Ont. Superior Court of Justice [Commercial List]

Air Canada, Re

2003 CarswellOnt 5296, [2003] O.J. No. 5319, 128 A.C.W.S. (3d) 9, 47 C.B.R. (4th) 163

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

AND IN THE MATTER OF SECTION 191 OF THE CANADA BUSINESS CORPORATIONS ACT, R.S.C. 1985, c.
C-44, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF AIR CANADA AND THOSE
SUBSIDIARIES LISTED ON SCHEDULE "A"

APPLICATION UNDER THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS
AMENDED

Farley J.

Heard: December 17, 2003

Judgment: December 17, 2003

Written reasons: December 21, 2003

Docket: 03-CL-4932

Counsel: David R. Byers, Timothy Banks, Karen Park for Applicants, Air Canada
James P. Dube, Susan M. Grundy for Lufthansa
Aubrey Kauffman for Ad Hoc Committee of Financial Creditors
Gregory Azeff for GECAS
A. Cobb for Trinity Time Investments Limited
Joseph Bellissimo for Ad Hoc Aircraft Lessor/Lender Group
Erik Penz for Unsecured Creditors Committee
Jeremy Dacks for GE Capital
Peter J. Osborne, Monique Jilesen for Monitor

Subject: Insolvency; Corporate and Commercial

Related Abridgment Classifications

For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Arrangements — Approval by court — "Fair and reasonable"

Debtor company AC was involved in proceedings under Companies' Creditors Arrangement Act — Certain bondholders objected to Canada-Germany Co-operation Agreement between AC and creditor LH on basis that AC and LH were attempting to have LH gain advantage over other creditors to which it was not otherwise entitled — Agreement was approved — Court must always be concerned that there not be ill-founded arm-twisting of debtor company such that debtor company and its creditors and other stakeholders are put to significant disadvantage — In exercising its discretion, court ought to take into account extent and nature of support of interested parties as to payment to critical vendor — Most creditors in this case approved Agreement — Relationship with LH had been extremely beneficial to AC and it was reasonably expected that benefit would continue to increase during currency of Agreement — Cost to AC of attempting to obtain even part of that benefit through alliances with other airlines would be high — Objective in dealing with creditors under Companies' Creditors Arrangement Act should be fair, reasonable and equitable treatment — Equitable treatment is not necessarily equal treatment — If Agreement were not approved and implemented, then AC and its creditors and stakeholders would probably be dealt severe blow which could well have devastating effect upon AC's chances of emerging successfully from Companies' Creditors Arrangement Act process.

Table of Authorities

Cases considered by *Farley J.*:

Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re (1999), 1999 CarswellOnt 3123 (Ont. S.C.J. [Commercial List]) — considered

Sammi Atlas Inc., Re (1998), 1998 CarswellOnt 1145, 3 C.B.R. (4th) 171 (Ont. Gen. Div. [Commercial List]) — considered

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3
Generally — referred to

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — considered

APPLICATION for approval of Agreement in course of proceedings under Companies' Creditors Arrangement Act.

Farley J.:

1 On December 17, 2003 at the end of the hearing, I wrote a very short Endorsement approving the Canada-Germany Co-operation Agreement ("Agreement") between Air Canada ("AC") and Deutsche Lufthansa Aktiengesellschaft ("LH") promising that I would provide reasons in due course. These are those reasons.

2 The Agreement was supported by all those appearing except for certain bondholders represented by Mr. Kauffman. His submissions were that AC and LH were attempting to have LH "gain an advantage over other creditors to which it is not otherwise entitled," indicating that this was being done in "precisely the same manner disapproved by Justice Blair" in *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re*, [1999] O.J. No. 3657 (Ont. S.C.J. [Commercial List]) at paragraph 10. The Court must always be concerned that there not be ill-founded arm-twisting of a CCAA applicant, such that the Applicant and its creditors and other stakeholders are put to a significant disadvantage. These concerns were generally addressed in the Report of the Insolvency Institute of Canada and Canadian Association of Insolvency and Restructuring Professionals Joint Task Force on Business Insolvency Law Reform of March 15, 2002 by recommendations 15-17. I attach a copy of those recommendations and the commentary as an appendix (Appendix "A") to these reasons. Perhaps it would be salutary if the critical vendor issue were addressed in a somewhat strengthened way if it were made clear that not more than, say one-half or one-third of a pre-filing debt could be "pressured out" of an applicant so that there might be some sharing of the pain by the critical vendor of what the other unsecured vendors were experiencing. Any such "pressured out" payment would leave to be accounted for in the plan of re-organization with respect to the balance of the debt which would be compromised. In any event, it would appear to me that in exercising its discretion, the Court ought to take into account the extent and nature of support of interested parties as to the payment to a critical vendor.

3 In the subject case, I find that the relationship with LH has been extremely beneficial to AC and it is reasonably expected that the benefit will continue to increase during the currency of the Agreement to 2009 and that the arrangements contemplated therein would likely not be possible to duplicate with any other airline (given LH's dominant position in Europe and its facility to be able to seamlessly be able to give AC's passengers to Eastern Europe and other promising areas of the world). Indeed, it would be extremely disruptive if the relationship were not continued. (LH indicated that it would terminate its relationship at the earliest opportunity if the Agreement were not approved). I note, in this regard that there was no direct evidence; however, there was no request for an adjournment or even cross-examination on the Brewer AC affidavit in this regard (which may suggest that Mr. Kauffman's concern here was more technical than practical - but he has a legitimate concern about this practice, which in my view is to be avoided in future absent justifiable and unusual circumstances). However, I do note that the Monitor in its 16th Report did not indicate that it had any concerns (after its extensive investigation of the situation) as to the legitimacy of the concern about the danger to AC or the *bona fides* of LH's caution.

4 The future net benefit to AC of the future arrangements and cooperation is expected to be substantial and considerably in excess of the pre-filing debt to LH which is to be paid over time pursuant to the terms of the Agreement.

5 The cost to AC to attempt to obtain even part of the benefit through alliances through other airlines, if possible, would be extremely expensive.

6 Taking these various factors into consideration, it is understandable that there was considerable support from the others taking part in this hearing. The Monitor has helpfully ruled out a potential double recovery issue vis-à-vis LH payments and the Kreditanstalt für Wiederaufbau ("KfW") loan transaction. These are documented by the LH and KfW letters at Tab C of

the Monitor's 16th Report.

7 In *Sammi Atlas Inc., Re* (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div. [Commercial List]), I observed at page 173 that, in dealing with creditors under the CCAA, equitable treatment is not necessarily equal treatment and that the objective should be fair, reasonable and equitable treatment.

8 With respect to *Red Cross, supra*, I note that the concern there of Blair, J. was that there was to be a lump sum payment out of the existing assets in what would be the CCAA Estate, which payment would diminish that estate out of which the other creditors would be paid. In contrast, the Agreement provides for payments to LH in the future and which are reasonably expected to be paid out of the future net profits guaranteed by AC and if the relationship with LH now consolidated and confirmed by the Agreement. See Blair, J.'s views in this regard at paragraphs 12-14:

¶ 12 . . . [R] egardless of the merits of the settlement as between its immediate parties or the apparent worthiness of its beneficiaries, I am not persuaded that a strong unsecured creditor and the debtor can effectively isolate a particular claim and carve it out of the CCAA proceedings by simple expedient of entering into an agreement purporting to settle their future relations.

¶ 13 The foregoing is premised, of course, on the lump sum payment which is made as part of the Settlement being paid out of a fund which is not a segregated trust fund and, therefor [sic], something outside of the CCAA proceedings

¶ 14 . . . In my view, it must be determined, however, before approval can be given to the pay equity settlement. If the Homemakers' Fund from which the \$10.2 million payment is to be made is, indeed, a segregated trust fund whose participants are agreeable to its being used for the purposes indicated, I would have no difficulty in approving the Settlement. Clearly it would be in the interests of the Red Cross, the Union and the employees in question, and all of the Red Cross Claimants to have the pay equity claim dealt with in the fashion proposed, if that were the case. In the absence of such a determination, however, I am not prepared to grant such approval, for the reasons articulated above (emphasis added).

9 In the result, I am of the view that the truly extraordinary and indeed it seems to me unique relationship of LH and AC which is so beneficial to AC and reasonably expected to be even more so in the future is to the overall benefit of the creditors and stakeholders of AC generally. If it were not approved and implemented, then AC and its creditors and stakeholders would probably be dealt a severe body blow which could well have a devastating effect upon the question of AC successfully emerging from this CCAA process. The Agreement is therefore approved.

10 Appendix attached.

Order accordingly.

Appendix — "A"

15. Provide (in both CCAA and BIA proposal cases) that no payments are to be made or security granted with respect to pre-filing unsecured claims without prior court approval (obtained after the initial order), except that with the prior written consent of the monitor/trustee (unless otherwise ordered by the court) the following pre-filing claims can be paid:

- (a) source deductions;
- (b) wages (including accrued vacation pay), benefits and sales tax remittances not yet due or not more than seven (7) days overdue at the date of filing; and
- (c) reasonable professional fees (subject to subsequent assessment) incurred with respect to the filing.

16. Provide (in both CCAA and BIA proposal cases) that no payments are to be made or additional security granted with respect to pre-filing secured claims (including security leases) that are subject to the stay without the prior approval of the court.

17. Provide that during a reorganization proceeding if there is no readily available alternative source of reasonably equivalent supply, then in order to prevent hostage payments the court has jurisdiction, on notice to the affected persons, to order any existing critical suppliers of goods and services (even though not under pre-filing contractual obligation to provide goods or services) to supply the debtor during the reorganization proceeding on normal pricing terms so long as effective arrangements are made to assure payment for post-filing supplies.

These three proposals complement one another and balance a prohibition on payment of pre-filing claims with important carve outs to recognize particular needs and interests. Proposal #15 prohibits payments being made or security granted to pre-filing unsecured claims without prior court approval. This prohibits the debtor from giving a preference to unsecured creditors, to the prejudice of more senior creditors or other unsecured creditors. However, the recommendation also recognizes that there are circumstances where it is in the interests of the debtor company as well as the general body of creditors to make payments. These include source deductions such as income tax, employment insurance and pension deductions, wages, accrued vacation pay, benefits and sales tax remittances that are not yet due or not more than 7 days overdue when the debtor files its application. In such cases, the debtor corporation, with the prior written consent of the monitor or trustee, can pay the claims without the cost and delay of having to obtain a court order.

This meets fairness objectives in that employees are being paid specified amounts and will be encouraged to stay through the restructuring. Tax remittances held in trust can also be paid for a limited period. The monitor or trustee acts as a check on behalf of the court and the general body of creditors in approving the payments. The debtor can go to the court if it believes that the monitor or trustee is withholding consent without valid reason.

The debtor would also be permitted to pay reasonable professional fees incurred with respect to the filing, also with the prior written consent of the monitor or trustee and subject to subsequent assessment by the court. This will facilitate timely filing of CCAA applications and commencement of the restructuring negotiations, and should prevent excessive appearances before the court. The subsequent assessment condition provides creditors with an avenue to object to these payments if they believe that they are excessive or unreasonable.

Proposal #16 is a prohibition on payments to be made or additional security to be granted to pre-filing secured creditors. This is aimed at ensuring both that a preference is not given to one or more secured creditors and that such creditors are not in a position to extract hostage payments from the debtor company during the stay period. Thus it is aimed at protection of the general body of creditors. Payments can be made or additional security granted if the court gives prior approval. Thus the general prohibition is tempered by granting the court discretion in its supervisory capacity to approve payments or security where appropriate.

Proposal #17 then recognizes that there may be instances in which there is no readily available alternate source of supply that is reasonably equivalent to the goods or services of a particular supplier. In order to prevent that creditor from extracting hostage payments during the restructuring proceeding, i.e. from demanding credit on excessive terms because the debtor has no ability to contract with another supplier, the recommendation puts in place a mechanism for the court to supervise the issue of continued supply of goods and services. The court would have the jurisdiction, on notice to the affected persons, to order an existing critical supplier of goods and services, even where it was not under a pre-filing contractual obligation to

continue supplying, to supply the debtor company during the reorganization proceeding. The court would have authority to order this on normal pricing terms, as long as effective arrangements were made to ensure payment for post-filing supplies. Thus the creditor would be required to continue to supply for a fixed period on normal pricing terms, but it would not be required to accept normal payment terms and the arrangement for payment by the debtor would have to satisfy the court that it was effective and timely. If the supplier had legitimate reasons for refusing to supply or for requesting increased pricing (for example, in order to recover extraordinary costs), the court would have authority to protect the supplier.

These three proposals together allow the debtor some discretion in respect of allowing payments, under supervision of the court-appointed officer, while ensuring that the general body of creditors is protected from the debtor preferring pre-existing creditors or being held hostage by a critical supplier. The fairness objectives are that it allows the debtor to continue to receive needed supplies and services, while balancing the interests and prejudice to other creditors. In terms of efficiency objectives, there is likely to be need for fewer court appearances if all stakeholders, including court-appointed officers and creditors, are given clear guidelines on the scope and ability to make payments or grant additional security during the stay period.

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Tab D

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

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF NORTEL NETWORKS CORPORATION, NORTEL NETWORKS LIMITED, NORTEL NETWORKS GLOBAL CORPORATION, NORTEL NETWORKS INTERNATIONAL CORPORATION AND NORTEL NETWORKS TECHNOLOGY CORPORATION

Applicants

APPLICATION UNDER THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

BEFORE: MORAWETZ J.

COUNSEL: Barry Wadsworth for the CAW and George Borosh et al

Susan Philpott and Mark Zigler for the Nortel Networks Former Employees

Lyndon Barnes and Adam Hirsh for the Nortel Networks Board of Directors

Alan Mersky and Mario Forte for Nortel Networks et al

Gavin H. Finlayson for the Informal Nortel Noteholders Group

Leanne Williams for Flextronics Inc.

Joseph Pasquariello and Chris Armstrong for Ernst & Young Inc., Monitor

Janice Payne for Recently Severed Canadian Nortel Employees (“RSCNE”)

Gail Misra for the CEP Union

**J. Davis-Sydor for Brookfield Lepage Johnson Controls Facility
Management Services**

**Henry Juroviesky for the Nortel Terminated Canadian Employees Steering
Committee**

Alex MacFarlane for the Official Unsecured Creditors Committee

M. Starnino for the Superintendent of Financial Services

HEARD: April 21, 2009

ENDORSEMENT

[1] The process by which claims of employees, both unionized and non-unionized, have been addressed in restructurings initiated under the *Companies’ Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the “CCAA”) has been the subject of debate for a number of years. There is uncertainty and strong divergent views have been expressed. Notwithstanding that employee claims are ultimately addressed in many CCAA proceedings, there are few reported decisions which address a number of the issues being raised in these two motions. This lack of jurisprudence may reflect that the issues, for the most part, have been resolved through negotiation, as opposed to being determined by the court in the CCAA process – which includes motions for directions, the classification of creditors’ claims, the holding and conduct of creditors’ meetings and motions to sanction a plan of compromise or arrangement.

[2] In this case, both unionized and non-unionized employee groups have brought motions for directions. This endorsement addresses both motions.

Union Motion

[3] The first motion is brought by the National Automobile, Aerospace, Transportation and General Workers Union of Canada (CAW – Canada) and its Locals 27, 1525, 1530, 1535, 1837, 1839, 1905, and/or 1915 (the “Union”) and by George Borosh on his own behalf and on behalf of all retirees of the Applicants who were formerly represented by the Union.

[4] The Union requests an order directing the Applicants (also referred to as “Nortel”) to recommence certain periodic and lump sum payments which the Applicants, or any of them, are obligated to make pursuant to the CAW collective agreement (the “Collective Agreement”). The Union also seeks an order requiring the Applicants to pay to those entitled persons the payments which should have been made to them under the Collective Agreement since January 14, 2009, the date of the CCAA filing and the date of the Initial Order.

[5] The Union seeks continued payment of certain of these benefits including:

- (a) retirement allowance payments (“RAP”);
- (b) voluntary retirement options (“VRO”); and
- (c) termination and severance payments.

[6] The amounts claimed by the Union are contractual entitlements under the Collective Agreement, which the Union submits are payable only after an individual’s employment with the Applicants has ceased.

[7] There are approximately 101 former Union members with claims to RAP. The current value of these RAP is approximately \$2.3 million. There are approximately 180 former unionized retirees who claim similar benefits under other collective agreements.

[8] There are approximately 7 persons who may assert claims to VRO as of the date of the Initial Order. These claims amount to approximately \$202,000.

[9] There are also approximately 600 persons who may claim termination and severance pay amounts. Five of those persons are former union members.

Former Employee Motion

[10] The second motion is brought by Mr. Donald Sproule, Mr. David Archibald and Mr. Michael Campbell (collectively, the “Representatives”) on behalf of former employees, including pensioners, of the Applicants or any person claiming an interest under or on behalf of such former employees or pensioners and surviving spouses in receipt of a Nortel pension, or group or class of them (collectively, the “Former Employees”). The Representatives seek an order varying the Initial Order by requiring the Applicants to pay termination pay, severance pay, vacation pay and an amount equivalent to the continuation of the benefit plans during the notice period, which are required to be paid to affected Former Employees in accordance with the *Employment Standards Act, 2000* S.O. 2000 c.41 (“ESA”) or any other relevant provincial employment legislation. The Representatives also seek an order varying the Initial Order by requiring the Applicants to recommence certain periodic and lump sum payments and to make payment of all periodic and lump sum payments which should have been paid since the Initial Order, which the Applicants are obligated to pay Former Employees in accordance with the statutory and contractual obligations entered into by Nortel and affected Former Employees, including the Transitional Retirement Allowance (“TRA”) and any pension benefit payments

Former Employees are entitled to receive in excess of the Nortel Networks Limited Managerial and Non-negotiated Pension Plan (the "Pension Plan"). TRA is similar to RAP, but is for non-unionized retirees. There are approximately 442 individuals who may claim the TRA. The current value of TRA obligations is approximately \$18 million.

[11] The TRA and the RAP are both unregistered benefits that run concurrently with other pension entitlements and operate as time-limited supplements.

[12] In many respects, the motion of the Former Employees is not dissimilar to the CAW motion, such that the motion of the Former Employees can almost be described as a "Me too motion".

Background

[13] On January 14, 2009, the Applicants were granted protection under the CCAA, pursuant to the Initial Order.

[14] Upon commencement of the CCAA proceedings, the Applicants ceased making payments of amounts that constituted or would constitute unsecured claims against the Applicants. Included were payments for termination and severance, as well as amounts under various retirement and retirement transitioning programs.

[15] The Initial Order provides:

- (a) that Nortel is entitled but not required to pay, among other things, outstanding and future wages, salaries, vacation pay, employee benefits and pension plan payments;
- (b) that Nortel is entitled to terminate the employment of or lay off any of its employees and deal with the consequences under a future plan of arrangement;
- (c) that Nortel is entitled to vacate, abandon or quit the whole but not part of any lease agreement and repudiate agreements relating to leased properties (paragraph 11);
- (d) for a stay of proceedings against Nortel;
- (e) for a suspension of rights and remedies vis-à-vis Nortel;
- (f) that during the stay period no person shall discontinue, repudiate, cease to perform any contract, agreement held by the company (paragraph 16);
- (g) that those having agreements with Nortel for the supply of goods and/or services are restrained from, among other things, discontinuing, altering or terminating the supply of such goods or services. The proviso is that the goods or services

supplied are to be paid for by Nortel in accordance with the normal payment practices.

Position of Union

[16] The position of the CAW is that the Applicants' obligations to make the payments is to the CAW pursuant to the Collective Agreement. The obligation is not to the individual beneficiaries.

[17] The Union also submits that the difference between the moving parties is that RAP, VRO and other payments are made pursuant to the Collective Agreement as between the Union and the Applicants and not as an outstanding debt payable to former employees.

[18] The Union further submits that the Applicants are obligated to maintain the full measure of compensation under the Collective Agreement in exchange for the provision of services provided by the Union's members subsequent to the issuance of the Initial Order. As such, the failure to abide by the terms of the Collective Agreement, the Union submits, runs directly contrary to Section 11.3 of the CCAA as compensation paid to employees under a collective agreement can reasonably be interpreted as being payment for services within the meaning of this section.

[19] Section 11.3 of the CCAA provides:

No order made under section 11 shall have the effect of

- (a) prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided after the order is made; or
- (b) requiring the further advance of money or credit.

[20] In order to fit within Section 11.3, services have to be provided after the date of the Initial Order.

[21] The Union submits that persons owed severance pay are post-petition trade creditors in a bankruptcy, albeit in relation to specific circumstances. Thus, by analogy, persons owed severance pay are post-petition trade creditors in a CCAA proceeding. The Union relies on *Smokey River Coal Ltd. (Re)* 2001 ABCA 209 to support its proposition.

[22] The Union further submits that when interpreting "compensation" for services performed under the Collective Agreement, it must include all of the monetary aspects of the Collective Agreement and not those specifically made to those actively employed on any particular given day.

[23] The Union takes the position that Section 11.3 of the CCAA specifically contemplates that a supplier is entitled to payment for post-filing goods and services provided, and would

undoubtedly refuse to continue supply in the event of receiving only partial payment. However, the Union contends that it does not have the ability to cease providing services due to the *Labour Relations Act, 1995*, S.O. 1995, c. 1. As such, the only alternative open to the Union is to seek an order to recommence the payments halted by the Initial Order.

[24] The Union contends that Section 11.3 of the CCAA precludes the court from authorizing the Applicants to make selective determinations as to which parts of the Collective Agreement it will abide by. By failing to abide by the terms of the Collective Agreement, the Union contends that the Applicants have acted as if the contract has been amended to the extent that it is no longer bound by all of its terms and need merely address any loss through the plan of arrangement.

[25] The Union submits that, with the exception of rectification to clarify the intent of the parties, the court has no jurisdiction at common law or in equity to alter the terms of the contract between parties and as the court cannot amend the terms of the Collective Agreement, the employer should not be allowed to act as though it had done so.

[26] The Union submits that no other supplier of services would countenance, and the court does not have the jurisdiction to authorize, the recipient party to a contract unilaterally determining which provisions of the agreement it will or will not abide by while the contract is in operation.

[27] The Union concludes that the Applicants must pay for the full measure of its bargain with the Union while the Collective Agreement remains in force and the court should direct the recommencement and repayment of those benefits that arise out of the Collective Agreement and which were suspended subsequently to the filing of the CCAA application on January 14, 2009.

Position of the Former Employees

[28] Counsel to the Former Employees submits that the court has the discretion pursuant to Section 11 of the CCAA to order Nortel to recommence periodic and lump-sum payments to Former Employees in accordance with Nortel's statutory and contractual obligations. Further, the RAP payments which the Union seeks to enforce are not meaningfully different from those RAP benefits payable to other unionized retirees who belong to other unions nor from the TRA payable to non-unionized former employees. Accordingly, counsel submits that it would be inequitable to restore payments to one group of retirees and not others. Hence, the reference to the "Me too motion".

[29] Counsel further submits that all employers and employees are bound by the minimum standards in the ESA and other applicable provincial employment legislation. Section 5 of the ESA expressly states that no employer can contract out or waive an employment standard in the ESA and that any such contracting out or waiver is void.

[30] Counsel submits that each province has minimum standards employment legislation and regulations which govern employment relationships at the provincial level and that provincial laws such as the ESA continue to apply during CCAA proceedings.

[31] Further, the Supreme Court of Canada has held that provincial laws in federally-regulated bankruptcy and insolvency proceedings continue to apply so long as the doctrine of paramountcy is not triggered: See *Crystalline Investments Ltd. v. Domgroup Ltd.*, [2004] 1 S.C.R. 60.

[32] In this case, counsel further submits that there is no conflict between the provisions of the ESA and the CCAA and that paramountcy is not triggered and it follows that the ESA and other applicable employment legislation continues to apply during the Applicants' CCAA proceedings. As a result counsel submits that the Applicants are required to make payment to Former Employees for monies owing pursuant to the minimum employment standards as outlined in the ESA and other applicable provincial legislation.

Position of the Applicants

[33] Counsel to the Applicants sets out the central purpose of the CCAA as being: "to facilitate the making of a compromise or arrangement between an insolvent debtor company and its creditors to the end that the company is able to continue in business". (*Pacific National Lease Holding Corp. (Re)*, (1992) B.C.J. No. 3070, aff'd by 1992, 15 C.B.R. (3d) 265), and that the stay is the primary procedural instrument used to achieve the purpose of the CCAA:

...if the attempt at a compromise or arrangement is to have any prospect of success, there must be a means of holding the creditors at bay. Hence the powers vested in the court under Section 11 (*Pacific National Lease Holding Corp. (Re)*, *supra*).

[34] The Applicants go on to submit that the powers vested in the court under Section 11 to achieve these goals of the CCAA include:

- (a) the ability to stay past debts; and
- (b) the ability to require the continuance of present obligations to the debtor.

[35] The corresponding protection extended to persons doing business with the debtor is that such persons (including employees) are not required to extend credit to the debtor corporation in the course of the CCAA proceedings. The protection afforded by Section 11.3 extends only to services provided after the Initial Order. Post-filing payments are only made for the purpose of ensuring the continued supply of services and that obligations in connection with past services are stayed. (See *Mirant Canada Energy Marketing Ltd. (Re)* (2004), A.J. No. 331).

[36] Furthermore, counsel to the Applicants submits that contractual obligations respecting post employment are obligations in respect of past services and are accordingly stayed.

[37] Counsel to the Applicants also relies on the following statement from *Mirant, supra*, at paragraph 28:

Thus, for me to find the decision of the Court of Appeal in Smokey River Coal analogous to Schaefer's situation, I would need to find that the obligation to pay

severance pay to Schaefer was a clear contractual obligation that was necessary for Schaefer to continue his employment and not an obligation that arose from the cessation or termination of services. In my view, to find it to be the former would be to stretch the meaning of the obligation in the Letter Agreement to pay severance pay. It is an obligation that arises on the termination of services. It does not fall within a commercially reasonable contractual obligation essential for the continued supply of services. Only is his salary which he has been paid falls within that definition.

[38] Counsel to the Applicants states that post-employment benefits have been consistently stayed under the CCAA and that post-employment benefits are properly regarded as pre-filing debts, which receive the same treatment as other unsecured creditors. The Applicants rely on *Syndicat nationale de l'amiante d'Asbestos inc. v. Jeffrey Mines Inc.* (2003) Q.J. No. 264 (C.A.) ("*Jeffrey Mine*") for the proposition that "the fact that these benefits are provided for in the collective agreement changes nothing".

[39] Counsel to the Applicants submits that the Union seeks an order directing the Applicants to make payment of various post-employment benefits to former Nortel employees and that the Former Employees claim entitlement to similar treatment for all post-employment benefits, under the Collective Agreement or otherwise.

[40] The Applicants take the position the Union's continuing collective representation role does not clothe unpaid benefits with any higher status, relying on the following from *Jeffrey Mine* at paras. 57 – 58:

Within the framework of the restructuring plan, arrangements can be made respecting the amounts owing in this regard.

The same is true in the case of the loss of certain fringe benefits sustained by persons who have not provided services to the debtor since the initial order. These persons became creditors of the debtor for the monetary value of the benefits lost further to Jeffrey Mines Inc.'s having ceased to pay premiums. The fact that these benefits are provided for in the collective agreements changes nothing.

[41] In addition, the Applicants point to the following statement of the Quebec Court of Appeal in *Syndicat des employées et employés de CFAP-TV (TQS-Quebec), section locale 3946 du Syndicat canadien de la fonction publique c. TQS inc.*, 2008 QCCA 1429 at paras. 26-27:

[Unofficial translation] Employees' rights are defined by the collective agreement that governs them and by certain legislative provisions. However, the resulting claims are just as much [at] risk as those of other creditors, in this case suppliers whose livelihood is also threatened by the financial precariousness of their debtor.

The arguments of counsel for the Applicants are based on the erroneous premise that the employees are entitled to a privileged status. That is not what the CCAA provides nor is it what this court decided in *Syndicat national de l'amiante d'Asbestos inc. c. Mine Jeffrey inc.*

[42] Collectively, RAP payment and TRA payments entail obligations of over \$22 million. Counsel to the Applicants submits that there is no basis in principle to treat them differently. They are all stayed and there is no basis to treat any of these two unsecured obligations differently. The Applicants are attempting to restructure for the final benefit of all stakeholders and counsel submits that its collective resources must be used for such purposes.

Report of the Monitor

[43] In its Seventh Report, the Monitor notes that at the time of the Initial Order, the Applicants employed approximately 6,000 employees and had approximately 11,700 retirees or their survivors receiving pension and/or benefits from retirement plans sponsored by the Applicants.

[44] The Monitor goes on to report that the Applicants have continued to honour substantially all of the obligations to active employees. The Applicants have continued to make current service and special funding payments to their registered pension plans. All the health and welfare benefits for both active employees and retirees have been continued to be paid since the commencement of the CCAA proceedings.

[45] The Monitor further reports that at the filing date, payments to former employees for termination and severance as well as the provisions of the health and dental benefits ceased. In addition, non-registered and unfunded retirement plan payments ceased.

[46] More importantly, the Monitor reports that, as noted in previous Monitor's Reports, the Applicants' financial position is under pressure.

Discussion and Analysis

[47] The acknowledged purpose of the CCAA is to facilitate the making of a compromise or arrangement between an insolvent debtor company and its creditors to the end that the company is able to continue in business. (See *Pacific National Lease Holding Corp. (Re)*, (1992) B.C.J. No. 3070, aff'd by (1992), 15 C.B.R. (3d) 265, at para. 18 citing *Chef Ready Foods Ltd. v. Hongkong Bank of Canada* (1990), 4 C.B.R. (3d) 311 (B.C.C.A.) at 315). The primary procedural instrument used to achieve that goal is the ability of the court to issue a broad stay of proceedings under Section 11 of the CCAA.

[48] The powers vested in the court under Section 11 of the CCAA to achieve these goals include the ability to stay past debts; and the ability to require the continuance of present obligations to the debtor. (*Woodwards Limited (Re)*, (1993), 17 C.B.R. (3d) 236 (S.C.)).

[49] The Applicants acknowledged that they were insolvent in affidavit material filed on the Initial Hearing. This position was accepted and is referenced in my endorsement of January 14, 2009. The Applicants are in the process of restructuring but no plan of compromise or arrangement has yet to be put forward.

[50] The Monitor has reported that the Applicants are under financial pressure. Previous reports filed by the Monitor have provided considerable detail as to how the Applicants carry on operations and have provided specific information as to the interdependent relationship between Nortel entities in Canada, the United States, Europe, the Middle East and Asia.

[51] In my view, in considering the impact of these motions, it is both necessary and appropriate to take into account the overall financial position of the Applicants. There are several reasons for doing so:

- (a) The Applicants are not in a position to honour their obligations to all creditors.
- (b) The Applicants are in default of contractual obligations to a number of creditors, including with respect to significant bond issues. The obligations owed to bondholders are unsecured.
- (c) The Applicants are in default of certain obligations under the Collective Agreements.
- (d) The Applicants are in default of certain obligations owed to the Former Employees.

[52] It is also necessary to take into account that these motions have been brought prior to any determination of any creditor classifications. No claims procedure has been proposed. No meeting of creditors has been called and no plan of arrangement has been presented to the creditors for their consideration.

[53] There is no doubt that the views of the Union and the Former Employees differ from that of the Applicants. The Union insists that the Applicants honour the Collective Agreement. The Former Employees want treatment that is consistent with that being provided to the Union. The record also establishes that the financial predicament faced by retirees and Former Employees is, in many cases, serious. The record references examples where individuals are largely dependent upon the employee benefits that, until recently, they were receiving.

[54] However, the Applicants contend that since all of the employee obligations are unsecured it is improper to prefer retirees and the Former Employees over the other unsecured creditors of the Applicants and furthermore, the financial pressure facing the Applicants precludes them from paying all of these outstanding obligations.

[55] Counsel to the Union contends that the Applicants must pay for the full measure of its bargain with the Union while the Collective Agreement remains in force and further that the court does not have the jurisdiction to authorize a party, in this case the Applicants, to

unilaterally determine which provisions of the Collective Agreement they will abide by while the contract is in operation. Counsel further contends that Section 11.3 of the CCAA precludes the court from authorizing the Applicants to make selective determinations as to which parts of the Collective Agreement they will abide by and that by failing to abide by the terms of the Collective Agreement, the Applicants acted as if the Collective Agreement between themselves and the Union has been amended to the extent that the Applicants are no longer bound by all of its terms and need merely address any loss through the plan of arrangement.

[56] The Union specifically contends that the court has no jurisdiction to alter the terms of the Collective Agreement.

[57] In addressing these points, it is necessary to keep in mind that these CCAA proceedings are at a relatively early stage. It also must be kept in mind that the economic circumstances at Nortel are such that it cannot be considered to be carrying on "business as usual". As a result of the Applicants' insolvency, difficult choices will have to be made. These choices have to be made by all stakeholders.

[58] The Applicants have breached the Collective Agreement and, as a consequence, the Union has certain claims.

[59] However, the Applicants have also breached contractual agreements they have with Former Employees and other parties. These parties will also have claims as against the Applicants.

[60] An overriding consideration is that the employee claims whether put forth by the Union or the Former Employees, are unsecured claims. These claims do not have any statutory priority.

[61] In addition, there is nothing on the record which addresses the issue of how the claims of various parties will be treated in any plan of arrangement, nor is there any indication as to how the creditors will be classified. These issues are not before the court at this time.

[62] What is before the court is whether the Applicants should be directed to recommence certain periodic and lump sum payments that they are obligated to make under the Collective Agreement as well as similar or equivalent payments to Former Employees.

[63] It is necessary to consider the meaning of Section 11.3 and, in particular, whether the Section should be interpreted in the manner suggested by the Union.

[64] Counsel to the Union submits that the ordinary meaning of "services" in section 11.3 includes work performed by employees subject to a collective agreement. Further, even if the ordinary meaning is plain, courts must consider the purpose and scheme of the legislation, and relevant legal norms. Counsel submits that the courts must consider the entire context. As a result, when interpreting "compensation" for services performed under a collective agreement, counsel to the Union submits it must include all of the monetary aspects of the agreement and not those made specifically to those actively employed on any particular given day.

[65] No cases were cited in support of this interpretation.

[66] I am unable to agree with the Union's argument. In my view, section 11.3 is an exception to the general stay provision authorized by section 11 provided for in the Initial Order. As such, it seems to me that section 11.3 should be narrowly construed. (See Ruth Sullivan, *Sullivan on the Construction of Statutes*, 5th ed. (Markham, Ont.: LexisNexis Canada Inc., 2008) at 483-485.) Section 11.3 applies to services provided after the date of the Initial Order. The ordinary meaning of "services" must be considered in the context of the phrase "services, ... provided after the order is made". On a plain reading, it contemplates, in my view, some activity on behalf of the service provider which is performed after the date of the Initial Order. The CCAA contemplates that during the reorganization process, pre-filing debts are not paid, absent exceptional circumstances and services provided after the date of the Initial Order will be paid for the purpose of ensuring the continued supply of services.

[67] The flaw in the argument of the Union is that it equates the crystallization of a payment obligation under the Collective Agreement to a provision of a service within the meaning of s. 11.3. The triggering of the payment obligation may have arisen after the Initial Order but it does not follow that a service has been provided after the Initial Order. Section 11.3 contemplates, in my view, some current activity by a service provider post-filing that gives rise to a payment obligation post-filing. The distinction being that the claims of the Union for termination and severance pay are based, for the most part, on services that were provided pre-filing. Likewise, obligations for benefits arising from RAP and VRO are again based, for the most part, on services provided pre-filing. The exact time of when the payment obligation crystallized is not, in my view, the determining factor under section 11.3. Rather, the key factor is whether the employee performed services after the date of the Initial Order. If so, he or she is entitled to compensation benefits for such current service.

[68] The interpretation urged by counsel to the Union with respect to this section is not warranted. In my view, section 11.3 does not require the Applicants to make payment, at this time, of the outstanding obligations under the Collective Agreement.

[69] The Union also raised the issue as to whether the court has the jurisdiction to order a stay of the outstanding obligations under Section 11 of the CCAA.

[70] The Union takes the position that, with the exception of rectification to clarify the intent of the parties, the court has no jurisdiction at common law or in equity to alter the terms of a contract between parties. The Union relies on *Bilodeau et al v. McLean*, [1924] 3 D.L.R. 410 (Man. C.A.); *Desener v. Myles*, [1963] S. J. No. 31 (Q.B.); *Hiesinger v. Bonice* [1984] A. J. No. 281; *Werchola v. KC5 Amusement Holdings Ltd.* 2002 SKQB 339 to support its position.

[71] The Union extends this argument and submits that as the court cannot amend the terms of a collective agreement, the employer should not be allowed to act as though it had been.

[72] As a general rule, counsel to the Union submits, there is in place a comprehensive regime for the regulation of labour relations with specialized labour-relations tribunals having exclusive

jurisdiction to deal with legal and factual matters arising under labour legislation and no court should restrain any tribunal from proceeding to deal with such matters.

[73] However, as is clear from the context, these cases referenced at [70] are dealing with the ordinary situation in which there is no issue of insolvency. In this case, we are dealing with a group of companies which are insolvent and which have been accorded the protection of the CCAA. In my view, this insolvency context is an important distinguishing factor. The insolvency context requires that the stay provisions provided in the CCAA and the Initial Order must be given meaningful interpretation.

[74] There is authority for the proposition that, when exercising their authority under insolvency legislation, the courts may make, at the initial stage of a CCAA proceeding, orders regarding matters, but for the insolvent condition of the employer, would be dealt with pursuant to provincial labour legislation, and in most circumstances, by labour tribunals. In *Re: Pacific National Lease Holding Corp.* (1992) 15 C.B.R. (3d) 265 (B.C.C.A.), the issue involved the question whether a CCAA debtor company had to make statutory severance payments as was mandatory under the provincial employment standards legislation. MacFarlane J.A. stated at pp. 271-2:

It appears to me that an order which treats creditors alike is in accord with the purpose of the CCAA. Without the provisions of that statute the petitioner companies might soon be in bankruptcy, and the priority which the employees now have would be lost. The process provided by the CCAA is an interim one. Generally, it suspends but does not determine the ultimate rights of any creditor. In the end it may result in the rights of employees being protected, but in the meantime it preserves the status quo and protects all creditors while a reorganization is being attempted.

...

This case is not so much about the rights of employees as creditors, but the right of the court under the CCAA to serve not only the special interests of the directors and officers of the company but the broader constituency referred to in *Chef Ready Foods Ltd., supra*. Such a decision may invariably conflict with provincial legislation, but the broad purpose of the CCAA must be served.

[75] The *Jeffrey Mine* decision is also relevant. In my view, the *Jeffrey Mine* case does not appear to support the argument that the Collective Agreement is to be treated as being completely unaffected by CCAA proceedings. It seems to me that it is contemplated that rights under a collective agreement may be suspended during the CCAA proceedings. At paragraphs 60 – 62, the court said under the heading Recapitulation (in translation):

The collective agreements continue to apply like any contract of successive performance not modified by mutual agreement after the initial order or not disclaimed (assuming that to be possible in the case of collective agreements).

Neither the monitor nor the court can amend them unilaterally. That said, distinctions need to be made with regard to the prospect of the resulting debts.

Thus, unionized employees kept on or recalled are entitled to be paid immediately by the monitor for any service provided after the date of the order (s. 11.3), in accordance with the terms of the original version of the applicable collective agreement by the union concerned. However, the obligations not honoured by Jeffrey Mine Inc. with regard to services provided prior to the order constitute debts of Jeffrey Mine Inc. for which the monitor cannot be held liable (s. 11.8 CCAA) and which the employees cannot demand to be paid immediately (s. 11.3 CCAA).

Obligations that have not been met with regard to employees who were laid off permanently on October 7, 2002, or with regard to persons who were former employees of Jeffrey Mine Inc. on that date and that stem from the collective agreements or other commitments constitute debts of the debtor to be disposed of in the restructuring plan or, failing that, upon the bankruptcy of Jeffrey Mine Inc.

[76] The issue of severance pay benefits was also referenced in *Communications, Energy, Paperworks, Local 721G v. Printwest Communications Ltd.* 2005 SKQB 331 at paras. 11 and 15. The application of the Union was rejected:

...The claims for severance pay arise from the collective bargaining agreement. But severance pay does not fall into the category of essential services provided during the organization period in order to enable Printwest to function.

...

If the Union's request should be accepted, with the result that the claims for severance pay be dealt with outside the plan of compromise – and thereby be paid in full – such a result could not possibly be viewed as fair and reasonable with respect to other unsecured creditors, who will possibly receive only a small fraction of the amounts owing to them for goods and services provided to Printwest in good faith. Thus, the application of the Union in this respect must be rejected.

Disposition

[77] At the commencement of an insolvency process, the situation is oftentimes fluid. An insolvent debtor is faced with many uncertainties. The statute is aimed at facilitating a plan of compromise or arrangement. This may require adjustments to the operations in a number of areas, one of which may be a downsizing of operations which may involve a reduction in the workforce. These adjustments may be painful but at the same time may be unavoidable. The alternative could very well be a bankruptcy which would leave former employees, both unionized and non-unionized, in the position of having unsecured claims against a bankrupt

debtor. Depending on the status of secured claims, these unsecured claims may, subject to benefits arising from the recently enacted *Wage Earner Protection Program Act*, be worth next to nothing.

[78] In the days ahead, the Applicants, former employees, both unionized and non-unionized may very well have arguments to make on issues involving claims processes (including the ability of the Applicants to compromise claims), classification, meeting of creditors and plan sanction. Nothing in this endorsement is intended to restrict the rights of any party to raise these issues.

[79] The reorganization process under the CCAA can be both long and painful. Ultimately, however, for a plan to be sanctioned by the court, the application must meet the following three tests:

- (i) there has to be strict compliance with all statutory requirements and adherence to previous orders of the court;
- (ii) nothing has been done or purported to be done that is not authorized by the CCAA;
- (iii) the plan is fair and reasonable. *Re: Sammi Atlas Inc.* (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div.)

[80] At this stage of the Applicants' CCAA process, I see no basis in principle to treat either unionized or non-unionized employees differently than other unsecured creditors of the Applicants. Their claims are all stayed. The Applicants are attempting to restructure for the benefit of all stakeholders and their resources should be used for such a purpose.

[81] It follows that the motion of the Union is dismissed.

[82] The Applicants also raised the issue that the Union consistently requested the right to bargain on behalf of retirees who were once part of the Union and that the concession had not been granted. Consequently, the retirees' substantive rights are not part of the bargain between the unionized employees and the employer. Counsel to the Applicants submitted that the union may collectively alter the existing rights of any employee but it cannot negatively do so with respect to retirees' rights.

[83] The Union countered that the rights gained by a member of the bargaining unit vest upon retirement, despite the fact that a collective agreement expires, and are enforceable through the grievance procedure.

[84] Both parties cited *Dayco (Canada) Ltd. v. National Automobile, Aerospace and Agricultural Implement Workers Union of Canada (CAW-Canada)* [1993] 2 S.C.R. 230 in support of their respective positions.

[85] In view of the fact that this motion has been dismissed for other reasons, it is not necessary for me to determine this specific issue arising out of the *Dayco* decision.

[86] The motion of the Former Employees was characterized, as noted above, as a “Me too motion”. It was based on the premise that, if the Union’s motion was successful, it would only be equitable if the Former Employees also received benefits. The Former Employees do not have the benefit of any enhanced argument based on the Collective Agreement. Rather, the argument of the Former Employees is based on the position that the Applicants cannot contract out of the ESA or any other provincial equivalent. In my view, this is not a case of contracting out of the ESA. Rather, it is a case of whether immediate payout resulting from a breach of the ESA is required to be made. In my view, the analysis is not dissimilar from the Collective Agreement scenario. There is an acknowledgment of the applicability of the ESA, but during the stay period, the Former Employees cannot enforce the payment obligation. In the result, it follows that the motion of the Former Employees is also dismissed.

[87] However, I am also mindful that the record, as I have previously noted, makes reference to a number of individuals that are severely impacted by the cessation of payments. There are no significant secured creditors of the Applicants, outside of certain charges provided for in the CCAA proceedings, and in view of the Applicants’ declared assets, it is reasonable to expect that there will be a meaningful distribution to unsecured creditors, including retirees and Former Employees. The timing of such distribution may be extremely important to a number of retirees and Former Employees who have been severely impacted by the cessation of payments. In my view, it would be both helpful and equitable if a partial distribution could be made to affected employees on a timely basis.

[88] In recognition of the circumstances that face certain retirees and Former Employees, the Monitor is directed to review the current financial circumstances of the Applicants and report back as to whether it is feasible to establish a process by which certain creditors, upon demonstrating hardship, could qualify for an unspecified partial distribution in advance of a general distribution to creditors. I would ask that the Monitor consider and report back to this court on this issue within 30 days.

[89] This decision may very well have an incidental effect on the Collective Agreement and the provisions of the ESA, but it is one which arises from the stay. It does not, in my view, result from a repudiation of the Collective Agreement or a contracting out of the ESA. The stay which is being recognized is, in my view, necessary in the circumstances. To hold otherwise, would have the effect of frustrating the objectives of the CCAA to the detriment of all stakeholders.

MORAWETZ J.

DATE: **June 18, 2009**

Tab E

2010 ONSC 1708
Ontario Superior Court of Justice [Commercial List]

Nortel Networks Corp., Re

2010 CarswellOnt 1754, 2010 ONSC 1708, 192 A.C.W.S. (3d) 368, 63 C.B.R. (5th) 44, 81 C.C.P.B. 56

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF NORTEL NETWORKS CORPORATION, NORTEL NETWORKS LIMITED, NORTEL NETWORKS GLOBAL CORPORATION, NORTEL NETWORKS INTERNATIONAL CORPORATION AND NORTEL NETWORKS TECHNOLOGY CORPORATION
(Applicants)

Morawetz J.

Heard: March 3-5, 2010
Judgment: March 26, 2010
Docket: 09-CL-7950

Counsel: Derrick Tay, Jennifer Stam, Suzanne Wood for Applicants
Lyndon Barnes, Adam Hirsh for Nortel Directors
Benjamin Zarnett, Gale Rubenstein, C. Armstrong, Melaney Wagner for Monitor, Ernst & Young Inc.
Arthur O. Jacques for Nortel Canada Current Employees
Deborah McPhail for Superintendent of Financial Services (non-PBGF)
Mark Zigler, Susan Philpott for Former and Long-Term Disability Employees
Ken Rosenberg, M. Starnino for Superintendent of Financial Services in its capacity as Administrator of the Pension Benefit Guarantee Fund
S. Richard Orzy, Richard B. Swan for Informal Nortel Noteholder Group
Alex MacFarlane, Mark Dunsmuir for Unsecured Creditors' Committee of Nortel Networks Inc.
Leanne Williams for Flextronics Inc.
Barry Wadsworth for CAW-Canada
Pamela Huff for Northern Trust Company, Canada
Joel P. Rochon, Sakie Tambakos for Opposing Former and Long-Term Disability Employees
Robin B. Schwill for Nortel Networks UK Limited (In Administration)
Sorin Gabriel Radulescu for himself
Guy Martin for himself, Marie Josee Perrault
Peter Burns for himself
Stan and Barbara Arnelien for themselves

Subject: Insolvency; Corporate and Commercial; Civil Practice and Procedure

Related Abridgment Classifications

For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Arrangements — Approval by court — “Fair and reasonable”

N Corp. was insolvent major telecommunications company which continued to provide pension and other benefits to former employees, retired employees (retirees) and employees on long-term disability (LTD employees) on discretionary basis — N Corp. was granted stay of proceedings under Companies' Creditors Arrangement Act (CCCA), but cessation of payments was inevitable — To reduce or eliminate uncertainty, risk of litigation and disruption in transition of benefits and to provide for early payments to terminated employees and maintain quantum and validity of pension and health and welfare trust (HWT) claims as ordinary, unsecured claims, N Corp. negotiated settlement agreement (SA) with Monitor appointed under CCAA, representatives of former employees, LTD employees and settlement counsel, and union — SA provided, among other things, for funding and payment of pensions and benefits under HWT until specified dates, for ranking of allowable pension claims *pari passu* with claims of unsecured creditors, and for express exclusion of HWT benefits from preferential or priority claim or trust — SA contained Bankruptcy and Insolvency Act (BIA) clause providing that subsequent amendments to BIA changing current, relative priorities of claims against N Corp. did not preclude party to SA from arguing applicability of amendment to claims ceded in SA — While most parties supported SA, committee of N Corp.'s unsecured creditors (Committee) and informal N Corp. noteholder group (Noteholders) opposed SA on basis of BIA clause — Applicants brought motion for court approval of SA — Motion dismissed — SA was consistent with spirit and purpose of CCAA but could not be approved in current form as BIA clause in SA was not fair and reasonable in circumstances and resulted in agreement that provided neither certainty nor finality of fundamental priority issue — BIA clause created uncertainty and potential for fundamental alteration of SA — Practical effect of BIA clause was that issue was not fully resolved and clause was somewhat inequitable to other unsecured creditors who were entitled to know, with certainty and finality, effect of SA — Comprehensive settlement of claims in magnitude and complexity contemplated by SA should not provide opportunity to re-trade deal after fact — BIA clause failed to recognize interests of other creditors whose claims ranked equally with claims of former employees and LTD employees — Effect of SA was to give former and LTD employees preferred treatment for certain claims, notwithstanding that priority was not provided for in statute and was not recognized in case law.

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Arrangements — Approval by court — Creditor approval

N Corp. was insolvent major telecommunications company which continued to provide pension and other benefits to former employees, retired employees (retirees) and employees on long-term disability (LTD employees) on discretionary basis — N Corp. was granted stay of proceedings under Companies' Creditors Arrangement Act (CCCA), but cessation of payments was inevitable — To reduce or eliminate uncertainty, risk of litigation and disruption in transition of benefits and to provide for early payments to terminated employees and maintain quantum and validity of pension and health and welfare trust (HWT) claims as ordinary, unsecured claims, N Corp. negotiated settlement agreement (SA) with Monitor appointed under CCAA, representatives of former employees, LTD employees and settlement counsel, and union — SA provided, among other things, for funding and payment of pensions and benefits under HWT until specified dates, for ranking of allowable pension claims *pari passu* with claims of unsecured creditors, and for express exclusion of HWT benefits from preferential or priority claim or trust — SA contained Bankruptcy and Insolvency Act (BIA) clause providing that subsequent amendments to BIA changing current, relative priorities of claims against N Corp. did not preclude party to SA from arguing applicability of amendment to claims ceded in SA — While most parties supported SA, committee of N Corp.'s unsecured creditors (Committee) and informal N Corp. noteholder group (Noteholders) opposed SA on basis of BIA clause — Applicants brought motion for court approval of SA — Motion dismissed — SA was consistent with spirit and purpose of CCAA but could not be approved in current form as BIA clause in SA was not fair and reasonable in circumstances and resulted in agreement that provided neither certainty nor finality of fundamental priority issue — BIA clause created uncertainty and potential for fundamental

alteration of SA — Practical effect of BIA clause was that issue was not fully resolved and clause was somewhat inequitable to other unsecured creditors who were entitled to know, with certainty and finality, effect of SA — Comprehensive settlement of claims in magnitude and complexity contemplated by SA should not provide opportunity to re-trade deal after fact — BIA clause failed to recognize interests of other creditors whose claims ranked equally with claims of former employees and LTD employees — Effect of SA was to give former and LTD employees preferred treatment for certain claims, notwithstanding that priority was not provided for in statute and was not recognized in case law.

Pensions --- Payment of pension --- Bankruptcy or insolvency of employer — Miscellaneous

N Corp. was insolvent major telecommunications company which continued to provide pension and other benefits to former employees, retired employees (retirees) and employees on long-term disability (LTD employees) on discretionary basis — N Corp. was granted stay of proceedings under Companies' Creditors Arrangement Act (CCCA), but cessation of payments was inevitable — To reduce or eliminate uncertainty, risk of litigation and disruption in transition of benefits and to provide for early payments to terminated employees and maintain quantum and validity of pension and health and welfare trust (HWT) claims as ordinary, unsecured claims, N Corp. negotiated settlement agreement (SA) with Monitor appointed under CCAA, representatives of former employees, LTD employees and settlement counsel, and union — SA provided, among other things, for funding and payment of pensions and benefits under HWT until specified dates, for ranking of allowable pension claims *pari passu* with claims of unsecured creditors, and for express exclusion of HWT benefits from preferential or priority claim or trust — SA contained Bankruptcy and Insolvency Act (BIA) clause providing that subsequent amendments to BIA changing current, relative priorities of claims against N Corp. did not preclude party to SA from arguing applicability of amendment to claims ceded in SA — While most parties supported SA, committee of N Corp.'s unsecured creditors (Committee) and informal N Corp. noteholder group (Noteholders) opposed SA on basis of BIA clause — Applicants brought motion for court approval of SA — Motion dismissed — SA was consistent with spirit and purpose of CCAA but could not be approved in current form as BIA clause in SA was not fair and reasonable in circumstances and resulted in agreement that provided neither certainty nor finality of fundamental priority issue — BIA clause created uncertainty and potential for fundamental alteration of SA — Practical effect of BIA clause was that issue was not fully resolved and clause was somewhat inequitable to other unsecured creditors who were entitled to know, with certainty and finality, effect of SA — Comprehensive settlement of claims in magnitude and complexity contemplated by SA should not provide opportunity to re-trade deal after fact — BIA clause failed to recognize interests of other creditors whose claims ranked equally with claims of former employees and LTD employees — Effect of SA was to give former and LTD employees preferred treatment for certain claims, notwithstanding that priority was not provided for in statute and was not recognized in case law.

Pensions --- Payment of pension --- Disability benefits

N Corp. was insolvent major telecommunications company which continued to provide pension and other benefits to former employees, retired employees (retirees) and employees on long-term disability (LTD employees) on discretionary basis — N Corp. was granted stay of proceedings under Companies' Creditors Arrangement Act (CCCA), but cessation of payments was inevitable — To reduce or eliminate uncertainty, risk of litigation and disruption in transition of benefits and to provide for early payments to terminated employees and maintain quantum and validity of pension and health and welfare trust (HWT) claims as ordinary, unsecured claims, N Corp. negotiated settlement agreement (SA) with Monitor appointed under CCAA, representatives of former employees, LTD employees and settlement counsel, and union — SA provided, among other things, for funding and payment of pensions and benefits under HWT until specified dates, for ranking of allowable pension claims *pari passu* with claims of unsecured creditors, and for express exclusion of HWT benefits from preferential or priority claim or trust — SA contained Bankruptcy and Insolvency Act (BIA) clause providing that subsequent amendments to BIA changing current, relative priorities of claims against N Corp. did not preclude party to SA from arguing applicability of amendment to claims ceded in SA — While most parties supported SA, committee of N Corp.'s unsecured creditors (Committee) and informal N Corp. noteholder group (Noteholders) opposed SA on basis of BIA clause — Applicants brought motion for court approval of SA — Motion dismissed — SA was consistent with spirit and purpose of CCAA but could not be approved in current form as BIA clause in SA was not fair and reasonable in circumstances and resulted in agreement that provided neither certainty nor finality of fundamental priority issue — BIA clause created uncertainty and potential for fundamental alteration of SA — Practical effect of BIA clause was that issue was not fully resolved and clause was somewhat inequitable to other unsecured creditors who were entitled to know, with certainty and finality, effect of SA —

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Nortel Networks Corp., Re (2009), 2009 CarswellOnt 4467, 55 C.B.R. (5th) 229 (Ont. S.C.J. [Commercial List]) — considered

Nortel Networks Corp., Re (2009), 2009 CarswellOnt 8166 (Ont. S.C.J. [Commercial List]) — referred to

Nortel Networks Corp., Re (2010), 2010 CarswellOnt 1044, 2010 ONSC 1096 (Ont. S.C.J. [Commercial List]) —

referred to

Stelco Inc., Re (2005), 204 O.A.C. 216, 78 O.R. (3d) 254, 2005 CarswellOnt 6283, 15 C.B.R. (5th) 288 (Ont. C.A.)
— considered

Wandlyn Inns Ltd., Re (1992), 15 C.B.R. (3d) 316, 1992 CarswellNB 37 (N.B. Q.B.) — considered

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3
Generally — referred to

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

s. 5.1(2) [en. 1997, c. 12, s. 122] — referred to

s. 11(4) — referred to

Pension Benefits Act, R.S.O. 1990, c. P.8
Generally — referred to

MOTION by insolvent corporation for court approval of settlement agreement under Companies' Creditors Arrangement Act.

Morawetz J.:

Introduction

1 On January 14, 2009, Nortel Networks Corporation ("NNC"), Nortel Networks Limited ("NNL"), Nortel Networks Global Corporation, Nortel Networks International Corporation and Nortel Networks Technology Corporation (collectively, the "Applicants") were granted a stay of proceedings pursuant to the *Companies' Creditors Arrangement Act* ("CCAA") and Ernst & Young Inc. was appointed as Monitor.

2 The Applicants have historically operated a number of pension, benefit and other plans (both funded and unfunded) for their employees and pensioners, including:

(i) Pension benefits through two registered pension plans, the Nortel Networks Limited Managerial and Non-Negotiated Pension Plan and the Nortel Networks Negotiated Pension Plan (the "Pension Plans"); and

(ii) Medical, dental, life insurance, long-term disability and survivor income and transition benefits paid, except for survivor termination benefits, through Nortel's Health and Welfare Trust (the "HWT").

3 Since the CCAA filing, the Applicants have continued to provide medical, dental and other benefits, through the HWT, to pensioners and employees on long-term disability ("Former and LTD Employees") and active employees ("HWT Payments") and have continued all current service contributions and special payments to the Pension Plans ("Pension Payments").

4 Pension Payments and HWT Payments made by the Applicants to the Former and LTD Employees while under CCAA protection are largely discretionary. As a result of Nortel's insolvency and the significant reduction in the size of Nortel's operations, the unfortunate reality is that, at some point, cessation of such payments is inevitable. The Applicants have attempted to address this situation by entering into a settlement agreement (the "Settlement Agreement") dated as of February 8, 2010, among the Applicants, the Monitor, the Former Employees' Representatives (on their own behalf and on behalf of the parties they represent), the LTD Representative (on her own behalf and on behalf of the parties she represents), Representative Settlement Counsel and the CAW-Canada (the "Settlement Parties").

5 The Applicants have brought this motion for approval of the Settlement Agreement. From the standpoint of the Applicants, the purpose of the Settlement Agreement is to provide for a smooth transition for the termination of Pension Payments and HWT Payments. The Applicants take the position that the Settlement Agreement represents the best efforts of the Settlement Parties to negotiate an agreement and is consistent with the spirit and purpose of the CCAA.

6 The essential terms of the Settlement Agreement are as follows:

(a) until December 31, 2010, medical, dental and life insurance benefits will be funded on a pay-as-you-go basis to the Former and LTD Employees;

(b) until December 31, 2010, LTD Employees and those entitled to receive survivor income benefits will receive income benefits on a pay-as-you-go basis;

(c) the Applicants will continue to make current service payments and special payments to the Pension Plans in the same manner as they have been doing over the course of the proceedings under the CCAA, through to March 31, 2010, in the aggregate amount of \$2,216,254 per month and that thereafter and through to September 30, 2010, the Applicants shall make only current service payments to the Pension Plans, in the aggregate amount of \$379,837 per month;

(d) any allowable pension claims, in these or subsequent proceedings, concerning any Nortel Worldwide Entity, including the Applicants, shall rank *pari passu* with ordinary, unsecured creditors of Nortel, and no part of any such HWT claims shall rank as a preferential or priority claim or shall be the subject of a constructive trust or trust of any nature or kind;

(e) proofs of claim asserting priority already filed by any of the Settlement Parties, or the Superintendent on behalf of the Pension Benefits Guarantee Fund are disallowed in regard to the claim for priority;

(f) any allowable HWT claims made in these or subsequent proceedings shall rank *pari passu* with ordinary unsecured creditors of Nortel;

(g) the Settlement Agreement does not extinguish the claims of the Former and LTD Employees;

(h) Nortel and, *inter alia*, its successors, advisors, directors and officers, are released from all future claims regarding Pension Plans and the HWT, provided that nothing in the release shall release a director of the Applicants from any matter referred to in subsection 5.1(2) of the CCAA or with respect to fraud on the part of any Releasee, with respect to that Releasee only;

(i) upon the expiry of all appeals and rights of appeal in respect thereof, Representative Settlement Counsel will

withdraw their application for leave to appeal the decision of the Court of Appeal, dated November 26, 2009, to the Supreme Court of Canada on a with prejudice basis;¹

(j) a CCAA plan of arrangement in the Nortel proceedings will not be proposed or approved if that plan does not treat the Pension and HWT claimants *pari passu* to the other ordinary, unsecured creditors ("Clause H.1"); and

(k) if there is a subsequent amendment to the *Bankruptcy and Insolvency Act* ("BIA") that "changes the current, relative priorities of the claims against Nortel, no party is precluded by this Settlement Agreement from arguing the applicability" of that amendment to the claims ceded in this Agreement ("Clause H.2").

7 The Settlement Agreement does *not* relate to a distribution of the HWT as the Settlement Parties have agreed to work towards developing a Court-approved distribution of the HWT corpus in 2010.

8 The Applicants' motion is supported by the Settlement Parties and by the Board of Directors of Nortel.

9 The Official Committee of Unsecured Creditors of Nortel Networks Inc. ("UCC"), the informal Nortel Noteholder Group (the "Noteholders"), and a group of 37 LTD Employees (the "Opposing LTD Employees") oppose the Settlement Agreement.

10 The UCC and Noteholders oppose the Settlement Agreement, principally as a result of the inclusion of Clause H.2.

11 The Opposing LTD Employees oppose the Settlement Agreement, principally as a result of the inclusion of the third party releases referenced in [6h] above.

The Facts

A. Status of Nortel's Restructuring

12 Although it was originally hoped that the Applicants would be able to restructure their business, in June 2009 the decision was made to change direction and pursue sales of Nortel's various businesses.

13 In response to Nortel's change in strategic direction and the impending sales, Nortel announced on August 14, 2009 a number of organizational updates and changes including the creation of groups to support transitional services and management during the sales process.

14 Since June 2009, Nortel has closed two major sales and announced a third. As a result of those transactions, approximately 13,000 Nortel employees have been or will be transferred to purchaser companies. That includes approximately 3,500 Canadian employees.

15 Due to the ongoing sales of Nortel's business units and the streamlining of Nortel's operations, it is expected that by the close of 2010, the Applicants' workforce will be reduced to only 475 employees. There is a need to wind-down and rationalize benefits and pension processes.

16 Given Nortel's insolvency, the significant reduction in Nortel's operations and the complexity and size of the Pension Plans, both Nortel and the Monitor believe that the continuation and funding of the Pension Plans and continued funding of medical, dental and other benefits is not a viable option.

B. The Settlement Agreement

17 On February 8, 2010 the Applicants announced that a settlement had been reached on issues related to the Pension Plans, and the HWT and certain employment related issues.

18 Recognizing the importance of providing notice to those who will be impacted by the Settlement Agreement, including the Former Employees, the LTD Employees, unionized employees, continuing employees and the provincial pension plan regulators ("Affected Parties"), Nortel brought a motion to this Court seeking the approval of an extensive notice and opposition process.

19 On February 9, 2010, this Court approved the notice program for the announcement and disclosure of the Settlement (the "Notice Order").

20 As more fully described in the Monitor's Thirty-Sixth, Thirty-Ninth and Thirty-Ninth Supplementary Reports, the Settlement Parties have taken a number of steps to notify the Affected Parties about the Settlement.

21 In addition to the Settlement Agreement, the Applicants, the Monitor and the Superintendent, in his capacity as administrator of the Pension Benefits Guarantee Fund, entered into a letter agreement on February 8, 2010, with respect to certain matters pertaining to the Pension Plans (the "Letter Agreement").

22 The Letter Agreement provides that the Superintendent will not oppose an order approving the Settlement Agreement ("Settlement Approval Order"). Additionally, the Monitor and the Applicants will take steps to complete an orderly transfer of the Pension Plans to a new administrator to be appointed by the Superintendent effective October 1, 2010. Finally, the Superintendent will not oppose any employee incentive program that the Monitor deems reasonable and necessary or the creation of a trust with respect to claims or potential claims against persons who accept directorships of a Nortel Worldwide Entity in order to facilitate the restructuring.

Positions of the Parties on the Settlement Agreement

The Applicants

23 The Applicants take the position that the Settlement is fair and reasonable and balances the interests of the parties and other affected constituencies equitably. In this regard, counsel submits that the Settlement:

- (a) eliminates uncertainty about the continuation and termination of benefits to pensioners, LTD Employees and survivors, thereby reducing hardship and disruption;
- (b) eliminates the risk of costly and protracted litigation regarding Pension Claims and HWT Claims, leading to reduced costs, uncertainty and potential disruption to the development of a Plan;
- (c) prevents disruption in the transition of benefits for current employees;
- (d) provides early payments to terminated employees in respect of their termination and severance claims where such employees would otherwise have had to wait for the completion of a claims process and distribution out of the estates;
- (e) assists with the commitment and retention of remaining employees essential to complete the Applicants' restructuring; and
- (f) does not eliminate Pension Claims or HWT Claims against the Applicants, but maintains their quantum and validity as ordinary and unsecured claims.

24 Alternatively, absent the approval of the Settlement Agreement, counsel to the Applicants submits that the Applicants are not required to honour such benefits or make such payments and such benefits could cease immediately. This would cause undue hardship to beneficiaries and increased uncertainty for the Applicants and other stakeholders.

25 The Applicants state that a central objective in the Settlement Agreement is to allow the Former and LTD Employees to transition to other sources of support.

26 In the absence of the approval of the Settlement Agreement or some other agreement, a cessation of benefits will occur on March 31, 2010 which would have an immediate negative impact on Former and LTD Employees. The Applicants submit that extending payments to the end of 2010 is the best available option to allow recipients to order their affairs.

27 Counsel to the Applicants submits that the Settlement Agreement brings Nortel closer to finalizing a plan of arrangement, which is consistent with the spirit and purpose of the CCAA. The Settlement Agreement resolves uncertainties associated with the outstanding Former and LTD Employee claims. The Settlement Agreement balances certainty with clarity, removing litigation risk over priority of claims, which properly balances the interests of the parties, including both creditors and debtors.

28 Regarding the priority of claims going forward, the Applicants submit that because a deemed trust, such as the HWT, is not enforceable in bankruptcy, the Former and LTD Employees are by default *pari passu* with other unsecured creditors.

29 In response to the Noteholders' concern that bankruptcy prior to October 2010 would create pension liabilities on the estate, the Applicants committed that they would not voluntarily enter into bankruptcy proceedings prior to October 2010. Further, counsel to the Applicants submits the court determines whether a bankruptcy order should be made if involuntary proceedings are commenced.

30 Further, counsel to the Applicants submits that the court has the jurisdiction to release third parties under a Settlement Agreement where the releases (1) are connected to a resolution of the debtor's claims, (2) will benefit creditors generally and (3) are not overly broad or offensive to public policy. See *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), 92 O.R. (3d) 513 (Ont. C.A.), [*Metcalfe*] at para. 71, leave to appeal refused, (S.C.C.) and *Grace Canada Inc., Re* (Ont. S.C.J. [Commercial List]) [*Grace 2008*] at para. 40.

31 The Applicants submit that a settlement of the type put forward should be approved if it is consistent with the spirit and purpose of the CCAA and is fair and reasonable in all the circumstances. Elements of fairness and reasonableness include balancing the interests of parties, including any objecting creditor or creditors, equitably (although not necessarily equally); and ensuring that the agreement is beneficial to the debtor and its stakeholders generally, as per *Air Canada, Re* (Ont. S.C.J. [Commercial List]) [*Air Canada*]. The Applicants assert that this test is met.

The Monitor

32 The Monitor supports the Settlement Agreement, submitting that it is necessary to allow the Applicants to wind down operations and to develop a plan of arrangement. The Monitor submits that the Settlement Agreement provides certainty, and does so with input from employee stakeholders. These stakeholders are represented by Employee Representatives as mandated by the court and these Employee Representatives were given the authority to approve such settlements on behalf of their constituents.

33 The Monitor submits that Clause H.2 was bargained for, and that the employees did give up rights in order to have that clause in the Settlement Agreement; particularly, it asserts that Clause H.1 is the counterpoint to Clause H.2. In this regard, the Settlement Agreement is fair and reasonable.

34 The Monitor asserts that the court may either (1) approve the Settlement Agreement, (2) not approve the Settlement Agreement, or (3) not approve the Settlement Agreement but provide practical comments on the applicability of Clause H.2.

Former and LTD Employees

35 The Former Employees' Representatives' constituents number an estimated 19,458 people. The LTD Employees number an estimated 350 people between the LTD Employee's Representative and the CAW-Canada, less the 37 people in the Opposing LTD Employee group.

36 Representative Counsel to the Former and LTD Employees acknowledges that Nortel is insolvent, and that much uncertainty and risk comes from insolvency. They urge that the Settlement Agreement be considered within the scope of this reality. The alternative to the Settlement Agreement is costly litigation and significant uncertainty.

37 Representative Counsel submits that the Settlement Agreement is fair and reasonable for all creditors, but especially

the represented employees. Counsel notes that employees under Nortel are unique creditors under these proceedings, as they are not sophisticated creditors and their personal welfare depends on receiving distributions from Nortel. The Former and LTD Employees assert that this is the best agreement they could have negotiated.

38 Representative Counsel submits that bargaining away of the right to litigate against directors and officers of the corporation, as well as the trustee of the HWT, are examples of the concessions that have been made. They also point to the giving up of the right to make priority claims upon distribution of Nortel's estate and the HWT, although the claim itself is not extinguished. In exchange, the Former and LTD Employees will receive guaranteed coverage until the end of 2010. The Former and LTD Employees submit that having money in hand today is better than uncertainty going forward, and that, on balance, this Settlement Agreement is fair and reasonable.

39 In response to allegations that third party releases unacceptably compromise employees' rights, Representative Counsel accepts that this was a concession, but submits that it was satisfactory because the claims given up are risky, costly and very uncertain. The releases do not go beyond s. 5.1(2) of the CCAA, which disallows releases relating to misrepresentations and wrongful or oppressive conduct by directors. Releases as to deemed trust claims are also very uncertain and were acceptably given up in exchange for other considerations.

40 The Former and LTD Employees submit that the inclusion of Clause H.2 was essential to their approval of the Settlement Agreement. They characterize Clause H.2 as a no prejudice clause to protect the employees by not releasing any future potential benefit. Removing Clause H.2 from the Settlement Agreement would be not the approval of an agreement, but rather the creation of an entirely new Settlement Agreement. Counsel submits that without Clause H.2, the Former and LTD Employees would not be signatories.

CAW

41 The CAW supports the Settlement Agreement. It characterizes the agreement as Nortel's recognition that it has a moral and legal obligation to its employees, whose rights are limited by the laws in this country. The Settlement Agreement temporarily alleviates the stress and uncertainty its constituents feel over the winding up of their benefits and is satisfied with this result.

42 The CAW notes that some members feel they were not properly apprised of the facts, but all available information has been disclosed, and the concessions made by the employee groups were not made lightly.

Board of Directors

43 The Board of Directors of Nortel supports the Settlement Agreement on the basis that it is a practical resolution with compromises on both sides.

Opposing LTD Employees

44 Mr. Rochon appeared as counsel for the Opposing LTD Employees, notwithstanding that these individuals did not opt out of having Representative Counsel or were represented by the CAW. The submissions of the Opposing LTD Employees were compelling and the court extends its appreciation to Mr. Rochon and his team in co-ordinating the representatives of this group.

45 The Opposing LTD Employees put forward the position that the cessation of their benefits will lead to extreme hardship. Counsel submits that the Settlement Agreement conflicts with the spirit and purpose of the CCAA because the LTD Employees are giving up legal rights in relation to a \$100 million shortfall of benefits. They urge the court to consider the unique circumstances of the LTD Employees as they are the people hardest hit by the cessation of benefits.

46 The Opposing LTD Employees assert that the HWT is a true trust, and submit that breaches of that trust create liabilities and that the claim should not be released. Specifically, they point to a \$37 million shortfall in the HWT that they should be able to pursue.

47 Regarding the third party releases, the Opposing LTD Employees assert that Nortel is attempting to avoid the distraction of third party litigation, rather than look out for the best interests of the Former and LTD Employees. The Opposing LTD Employees urge the court not to release the only individuals the Former and LTD Employees can hold accountable for any breaches of trust. Counsel submits that Nortel has a common law duty to fund the HWT, which the Former and LTD Employees should be allowed to pursue.

48 Counsel asserts that allowing these releases (a) is not necessary and essential to the restructuring of the debtor, (b) does not relate to the insolvency process, (c) is not required for the success of the Settlement Agreement, (d) does not meet the requirement that each party contribute to the plan in a material way and (e) is overly broad and therefore not fair and reasonable.

49 Finally, the Opposing LTD Employees oppose the *pari passu* treatment they will be subjected to under the Settlement Agreement, as they have a true trust which should grant them priority in the distribution process. Counsel was not able to provide legal authority for such a submission.

50 A number of Opposing LTD Employees made in person submissions. They do not share the view that Nortel will act in their best interests, nor do they feel that the Employee Representatives or Representative Counsel have acted in their best interests. They shared feelings of uncertainty, helplessness and despair. There is affidavit evidence that certain individuals will be unable to support themselves once their benefits run out, and they will not have time to order their affairs. They expressed frustration and disappointment in the CCAA process.

UCC

51 The UCC was appointed as the representative for creditors in the U.S. Chapter 11 proceedings. It represents creditors who have significant claims against the Applicants. The UCC opposes the motion, based on the inclusion of Clause H.2, but otherwise the UCC supports the Settlement Agreement.

52 Clause H.2, the UCC submits, removes the essential element of finality that a settlement agreement is supposed to include. The UCC characterizes Clause H.2 as a take back provision; if activated, the Former and LTD Employees have compromised nothing, to the detriment of other unsecured creditors. A reservation of rights removes the finality of the Settlement Agreement.

53 The UCC claims it, not Nortel, bears the risk of Clause H.2. As the largest unsecured creditor, counsel submits that a future change to the BIA could subsume the UCC's claim to the Former and LTD Employees and the UCC could end up with nothing at all, depending on Nortel's asset sales.

Noteholders

54 The Noteholders are significant creditors of the Applicants. The Noteholders oppose the settlement because of Clause H.2, for substantially the same reasons as the UCC.

55 Counsel to the Noteholders submits that the inclusion of H.2 is prejudicial to the non-employee unsecured creditors, including the Noteholders. Counsel submits that the effect of the Settlement Agreement is to elevate the Former and LTD Employees, providing them a payout of \$57 million over nine months while everyone else continues to wait, and preserves their rights in the event the laws are amended in future. Counsel to the Noteholders submits that the Noteholders forego millions of dollars while remaining exposed to future claims.

56 The Noteholders assert that a proper settlement agreement must have two elements: a real compromise, and resolution of the matters in contention. In this case, counsel submits that there is no resolution because there is no finality in that Clause H.2 creates ambiguity about the future. The very object of a Settlement Agreement, assert the Noteholders, is to avoid litigation by withdrawing claims, which this agreement does not do.

Superintendent

57 The Superintendent does not oppose the relief sought, but this position is based on the form of the Settlement Agreement that is before the Court.

Northern Trust

58 Northern Trust, the trustee of the pension plans and HWT, takes no position on the Settlement Agreement as it takes instructions from Nortel. Northern Trust indicates that an oversight left its name off the third party release and asks for an amendment to include it as a party released by the Settlement Agreement.

Law and Analysis

A. Representation and Notice Were Proper

59 It is well settled that the Former Employees' Representatives and the LTD Representative (collectively, the "Settlement Employee Representatives") and Representative Counsel have the authority to represent the Former Employees and the LTD Beneficiaries for purposes of entering into the Settlement Agreement on their behalf: *see Grace 2008, supra* at para 32.

60 The court appointed the Settlement Employee Representatives and the Representative Settlement Counsel. These appointment orders have not been varied or appealed. Unionized employees continue to be represented by the CAW. The Orders appointing the Settlement Employee Representatives expressly gave them authority to represent their constituencies "for the purpose of settling or compromising claims" in these Proceedings. Former Employees and LTD Employees were given the right to opt out of their representation by Representative Settlement Counsel. After provision of notice, only one former employee and one active employee exercised the opt-out right.

B. Effect of the Settlement Approval Order

61 In addition to the binding effect of the Settlement Agreement, many additional parties will be bound and affected by the Settlement Approval Order. Counsel to the Applicants submits that the binding nature of the Settlement Approval Order on all affected parties is a crucial element to the Settlement itself. In order to ensure all Affected Parties had notice, the Applicants obtained court approval of their proposed notice program.

62 Even absent such extensive noticing, virtually all employees of the Applicants are represented in these proceedings. In addition to the representative authority of the Settlement Employee Representatives and Representative Counsel as noted above, Orders were made authorizing a Nortel Canada Continuing Employees' Representative and Nortel Canada Continuing Employees' Representative Counsel to represent the interests of continuing employees on this motion.

63 I previously indicated that "the overriding objective of appointing representative counsel for employees is to ensure that the employees have representation in the CCAA process": *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]) at para 16. I am satisfied that this objective has been achieved.

64 The Record establishes that the Monitor has undertaken a comprehensive notice process which has included such notice to not only the Former Employees, the LTD Employees, the unionized employees and the continuing employees but also the provincial pension regulators and has given the opportunity for any affected person to file Notices of Appearance and appear before this court on this motion.

65 I am satisfied that the notice process was properly implemented by the Monitor.

66 I am satisfied that Representative Counsel has represented their constituents' interests in accordance with their mandate, specifically, in connection with the negotiation of the Settlement Agreement and the draft Settlement Approval Order and appearance on this Motion. There have been intense discussions, correspondence and negotiations among Representative Counsel, the Monitor, the Applicants, the Superintendent, counsel to the Board of the Applicants, the Noteholder Group and the Committee with a view to developing a comprehensive settlement. NCCE's Representative Counsel have been apprised of the settlement discussions and served with notice of this Motion. Representatives have held

Webinar sessions and published press releases to inform their constituents about the Settlement Agreement and this Motion.

C. Jurisdiction to Approve the Settlement Agreement

67 The CCAA is a flexible statute that is skeletal in nature. It has been described as a “sketch, an outline, a supporting framework for the resolution of corporate insolvencies in the public interest”. *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]) at paras. 28-29, citing *Metcalfe, supra*, at paras. 44 and 61.

68 Three sources for the court’s authority to approve pre-plan agreements have been recognized:

(a) the power of the court to impose terms and conditions on the granting of a stay under s. 11(4) of the CCAA;

(b) the power of the court to make an order “on such terms as it may impose” pursuant to s. 11(4) of the CCAA; and

(c) the inherent jurisdiction of the court to “fill in the gaps” of the CCAA in order to give effect to its objects: see *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]) at para. 30, citing *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (Ont. Gen. Div. [Commercial List]) [*Canadian Red Cross*] at para. 43; *Metcalfe, supra* at para. 44.

69 In *Stelco Inc., Re* (2005), 78 O.R. (3d) 254 (Ont. C.A.), the Ontario Court of Appeal considered the court’s jurisdiction under the CCAA to approve agreements, determining at para. 14 that it is not limited to preserving the *status quo*. Further, agreements made prior to the finalization of a plan or compromise are valid orders for the court to approve: *Grace 2008, supra* at para. 34.

70 In these proceedings, this court has confirmed its jurisdiction to approve major transactions, including settlement agreements, during the stay period defined in the Initial Order and prior to the proposal of any plan of compromise or arrangement: see, for example, *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]); *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]) and *Nortel Networks Corp., Re*, 2010 ONSC 1096 (Ont. S.C.J. [Commercial List]).

71 I am satisfied that this court has jurisdiction to approve transactions, including settlements, in the course of overseeing proceedings during a CCAA stay period and prior to any plan of arrangement being proposed to creditors: see *Calpine Canada Energy Ltd., Re* (Alta. C.A. [In Chambers]) [*Calpine*] at para. 23, affirming (Alta. Q.B.); *Canadian Red Cross, supra*; *Air Canada, supra*; *Grace 2008, supra*, and *Grace Canada Inc., Re* (Ont. S.C.J. [Commercial List]) [*Grace 2010*], leave to appeal to the C.A. refused February 19, 2010; *Nortel Networks Corp., Re*, 2010 ONSC 1096 (Ont. S.C.J. [Commercial List]).

D. Should the Settlement Agreement Be Approved?

72 Having been satisfied that this court has the jurisdiction to approve the Settlement Agreement, I must consider whether the Settlement Agreement *should* be approved.

73 A Settlement Agreement can be approved if it is consistent with the spirit and purpose of the CCAA and is fair and reasonable in all circumstances. What makes a settlement agreement fair and reasonable is its balancing of the interests of all parties; its equitable treatment of the parties, including creditors who are not signatories to a settlement agreement; and its benefit to the Applicant and its stakeholders generally.

i) Spirit and Purpose

74 The CCAA is a flexible instrument; part of its purpose is to allow debtors to balance the conflicting interests of stakeholders. The Former and LTD Employees are significant creditors and have a unique interest in the settlement of their claims. This Settlement Agreement brings these creditors closer to ultimate settlement while accommodating their special circumstances. It is consistent with the spirit and purpose of the CCAA.

ii) Balancing of Parties' Interests

75 There is no doubt that the Settlement Agreement is comprehensive and that it has support from a number of constituents when considered in its totality.

76 There is, however, opposition from certain constituents on two aspects of the proposed Settlement Agreement: (1) the Opposing LTD Employees take exception to the inclusion of the third party releases; (2) the UCC and Noteholder Groups take exception to the inclusion of Clause H.2.

Third Party Releases

77 Representative Counsel, after examining documentation pertaining to the Pension Plans and HWT, advised the Former Employees' Representatives and Disabled Employees' Representative that claims against directors of Nortel for failing to properly fund the Pension Plans were unlikely to succeed. Further, Representative Counsel advised that claims against directors or others named in the Third Party Releases to fund the Pension Plans were risky and could take years to resolve, perhaps unsuccessfully. This assisted the Former Employees' Representatives and the Disabled Employees' Representative in agreeing to the Third Party Releases.

78 The conclusions reached and the recommendations made by both the Monitor and Representative Counsel are consistent. They have been arrived at after considerable study of the issues and, in my view, it is appropriate to give significant weight to their positions.

79 In *Grace 2008, supra*, and *Grace 2010, supra*, I indicated that a Settlement Agreement entered into with Representative Counsel that contains third party releases is fair and reasonable where the releases are necessary and connected to a resolution of claims against the debtor, will benefit creditors generally and are not overly broad or offensive to public policy.

80 In this particular case, I am satisfied that the releases are necessary and connected to a resolution of claims against the

Applicants.

81 The releases benefit creditors generally as they reduces the risk of litigation against the Applicants and their directors, protect the Applicants against potential contribution claims and indemnity claims by certain parties, including directors, officers and the HWT Trustee; and reduce the risk of delay caused by potentially complex litigation and associated depletion of assets to fund potentially significant litigation costs.

82 Further, in my view, the releases are not overly broad or offensive to public policy. The claims being released specifically relate to the subject matter of the Settlement Agreement. The parties granting the release receive consideration in the form of both immediate compensation and the maintenance of their rights in respect to the distribution of claims.

Clause H.2

83 The second aspect of the Settlement Agreement that is opposed is the provision known as Clause H.2. Clause H.2 provides that, in the event of a bankruptcy of the Applicants, and notwithstanding any provision of the Settlement Agreement, if there are any amendments to the BIA that change the current, relative priorities of the claims against the Applicants, no party is precluded from arguing the applicability or non-applicability of any such amendment in relation to any such claim.

84 The Noteholders and UCC assert that Clause H.2 causes the Settlement Agreement to not be a “settlement” in the true and proper sense of that term due to a lack of certainty and finality. They emphasize that Clause H.2 has the effect of undercutting the essential compromises of the Settlement Agreement in imposing an unfair risk on the non-employee creditors of NNL, including NNI, after substantial consideration has been paid to the employees.

85 This position is, in my view, well founded. The inclusion of the Clause H.2 creates, rather than eliminates, uncertainty. It creates the potential for a fundamental alteration of the Settlement Agreement.

86 The effect of the Settlement Agreement is to give the Former and LTD Employees preferred treatment for certain claims, notwithstanding that priority is not provided for in the statute nor has it been recognized in case law. In exchange for this enhanced treatment, the Former Employees and LTD Beneficiaries have made certain concessions.

87 The Former and LTD Employees recognize that substantially all of these concessions could be clawed back through Clause H.2. Specifically, they acknowledge that future Pension and HWT Claims will rank *pari passu* with the claims of other ordinary unsecured creditors, but then go on to say that should the BIA be amended, they may assert once again a priority claim.

88 Clause H.2 results in an agreement that does not provide certainty and does not provide finality of a fundamental priority issue.

89 The Settlement Parties, as well as the Noteholders and the UCC, recognize that there are benefits associated with resolving a number of employee-related issues, but the practical effect of Clause H.2 is that the issue is not fully resolved. In my view, Clause H.2 is somewhat inequitable from the standpoint of the other unsecured creditors of the Applicants. If the creditors are to be bound by the Settlement Agreement, they are entitled to know, with certainty and finality, the effect of the Settlement Agreement.

90 It is not, in my view, reasonable to require creditors to, in effect, make concessions in favour of the Former and LTD Employees today, and be subject to the uncertainty of unknown legislation in the future.

91 One of the fundamental purposes of the CCAA is to facilitate a process for a compromise of debt. A compromise needs certainty and finality. Clause H.2 does not accomplish this objective. The inclusion of Clause H.2 does not recognize that at some point settlement negotiations cease and parties bound by the settlement have to accept the outcome. A comprehensive settlement of claims in the magnitude and complexity contemplated by the Settlement Agreement should not provide an opportunity to re-trade the deal after the fact.

92 The Settlement Agreement should be fair and reasonable in all the circumstances. It should balance the interests of the Settlement Parties and other affected constituencies equitably and should be beneficial to the Applicants and their stakeholders generally.

93 It seems to me that Clause H.2 fails to recognize the interests of the other creditors of the Applicants. These creditors have claims that rank equally with the claims of the Former Employees and LTD Employees. Each have unsecured claims against the Applicants. The Settlement Agreement provides for a transfer of funds to the benefit of the Former Employees and LTD Employees at the expense of the remaining creditors. The establishment of the Payments Charge crystallized this agreed upon preference, but Clause H.2 has the effect of not providing any certainty of outcome to the remaining creditors.

94 I do not consider Clause H.2 to be fair and reasonable in the circumstances.

95 In light of this conclusion, the Settlement Agreement cannot be approved in its current form.

96 Counsel to the Noteholder Group also made submissions that three other provisions of the Settlement Agreement were unreasonable and unfair, namely:

- (i) ongoing exposure to potential liability for pension claims if a bankruptcy order is made before October 1, 2010;
- (ii) provisions allowing payments made to employees to be credited against employees' claims made, rather than from future distributions or not to be credited at all; and
- (iii) lack of clarity as to whether the proposed order is binding on the Superintendent in all of his capacities under the *Pension Benefits Act* and other applicable law, and not merely in his capacity as Administrator on behalf of the Pension Benefits Guarantee Fund.

97 The third concern was resolved at the hearing with the acknowledgement by counsel to the Superintendent that the proposed order would be binding on the Superintendent in all of his capacities.

98 With respect to the concern regarding the potential liability for pension claims if a bankruptcy order is made prior to October 1, 2010, counsel for the Applicants undertook that the Applicants would not take any steps to file a voluntary assignment into bankruptcy prior to October 1, 2010. Although such acknowledgment does not bind creditors from commencing involuntary bankruptcy proceedings during this time period, the granting of any bankruptcy order is preceded by a court hearing. The Noteholders would be in a position to make submissions on this point, if so advised. This concern of the Noteholders is not one that would cause me to conclude that the Settlement Agreement was unreasonable and unfair.

99 Finally, the Noteholder Group raised concerns with respect to the provision which would allow payments made to employees to be credited against employees' claims made, rather than from future distributions, or not to be credited at all. I do not view this provision as being unreasonable and unfair. Rather, it is a term of the Settlement Agreement that has been negotiated by the Settlement Parties. I do note that the proposed treatment with respect to any payments does provide certainty and finality and, in my view, represents a reasonable compromise in the circumstances.

Disposition

100 I recognize that the proposed Settlement Agreement was arrived at after hard-fought and lengthy negotiations. There are many positive aspects of the Settlement Agreement. I have no doubt that the parties to the Settlement Agreement consider that it represents the best agreement achievable under the circumstances. However, it is my conclusion that the inclusion of Clause H.2 results in a flawed agreement that cannot be approved.

101 I am mindful of the submission of counsel to the Former and LTD Employees that if the Settlement Agreement were approved, with Clause H.2 excluded, this would substantively alter the Settlement Agreement and would, in effect, be a creation of a settlement and not the approval of one.

102 In addition, counsel to the Superintendent indicated that the approval of the Superintendent was limited to the proposed Settlement Agreement and would not constitute approval of any altered agreement.

103 In *Grace 2008, supra*, I commented that a line-by-line analysis was inappropriate and that approval of a settlement agreement was to be undertaken in its entirety or not at all, at para. 74. A similar position was taken by the New Brunswick Court of Queen's Bench in *Wandlyn Inns Limited (Re)* (1992), 15 C.B.R. (3d) 316 (N.B. Q.B.). I see no reason or basis to deviate from this position.

104 Accordingly, the motion is dismissed.

105 In view of the timing of the release of this decision and the functional funding deadline of March 31, 2010, the court will make every effort to accommodate the parties if further directions are required.

106 Finally, I would like to express my appreciation to all counsel and in person parties for the quality of written and oral submissions.

Motion dismissed.

Footnotes

¹ On March 25, 2010, the Supreme Court of Canada released the following: *Donald Sproule et al. v. Nortel Networks Corporation et al.* (Ont.) (Civil) (By Leave) (33491) (The motions for directions and to expedite the application for leave to appeal are dismissed. The application for leave to appeal is dismissed with no order as to costs./La requête en vue d'obtenir des directives et la requête visant à accélérer la procédure de demande d'autorisation d'appel sont rejetées. La demande d'autorisation d'appel est rejetée; aucune ordonnance n'est rendue concernant les dépens.); <http://scc.lexum.umontreal.ca/en/news_release/2010/10-03-25.3a/10-03-25.3a.html>