IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *Contech Enterprises Inc. (Re),* 2015 BCSC 129

Date: 20150126
Docket: B150025
Registry: Vancouver

In Bankruptcy and Insolvency

In the Matter of the Proposal of Contech Enterprises Inc.

Before: The Honourable Madam Justice S. Griffin

Oral Reasons for Judgment

Counsel for Contech Enterprises Inc. and Deloitte Restructuring Inc., Trustee:	Kibben M. Jackson, Danielle Toigo
Counsel for Vegherb, LLC:	Gregory N. Harney
Counsel for HSBC Bank Canada:	Bryan C. Gibbons
Place and Date of Hearing:	Vancouver, B.C. January 20 and 21, 2015
Place and Date of Judgment:	Vancouver, B.C. January 26, 2015

Introduction

[1] Contech Enterprises Inc. ("Contech") has filed a proposal under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 [*BIA*] (the "Proposal").

[2] One of its creditors is Vegherb LLC ("Vegherb"). Vegherb opposes approval of the Proposal.

[3] Another creditor is HSBC Bank Canada ("HSBC") which supports the Proposal.

[4] There are three applications before me:

a) Deloitte Restructuring Inc. (the "Trustee") in its capacity as trustee in bankruptcy of Contech and Contech seek an order approving the Proposal.

b) Contech seeks an order declaring that on fulfillment of the Proposal, it will be owner of certain intellectual property (the "IP") which was part of a past transaction whereby Contech purchased the assets of Vegherb. Vegherb opposes the application.

c) Vegherb seeks an order in the alternative that if the Proposal is approved, Vegherb be permitted to amend its proof of claim to change its position from that of a secured creditor to that of an unsecured creditor. Contech opposes the application.

[5] There is some urgency to the determination of these applications as Contech's position is that these issues need to be decided in order to complete a financing due to close on January 31, 2015. The financing will support the Proposal and is designed to keep Contech alive as a going concern. Contech says if the financing does not go ahead, the Proposal will fail and Contech will go into bankruptcy, and its assets will be liquidated, prejudicing many creditors as well as employees of Contech.

[6] Because of the urgency, these Reasons for Judgment will be brief in respect of some issues. I have borrowed from the submissions and application and response materials where I agreed with the content. If I fail to address an issue raised in the extensive submissions it is either because I did not consider it material or I did not consider it of any merit.

[7] I will deal with the application regarding the IP first as the dispute on this issue is key to all of the applications.

[8] Before I do so I will review the background facts.

Background

[9] Contech was founded in 1987 and carries on business as a designer, manufacturer and retailer of environmentally friendly products for the pet and garden industries. Contech has approximately 30 employees in Canada. Through a wholly owned U.S. subsidiary, Contech has an additional 35 employees in the U.S.

[10] The Trustee reports that in recent years Contech has expanded rapidly through its acquisitions of the shares and assets of other companies and persons.

[11] As part of Contech's acquisitions it purchased the assets of Vegherb approximately two years ago, in February 2013. Vegherb was in the business of developing, manufacturing and selling raised garden beds and sandboxes.

[12] The purchase price for Vegherb's assets was payable in part in cash to Vegherb or its creditors, in part by cash instalments, and in part by provision of Contech shares. The cash instalments were secured by a Promissory Note and a General Security Agreement granted by Contech over all of its personal property. Not all of the cash installments have been paid.

[13] There is an issue as to whether or not a License Agreement dealing with the Vegherb intellectual property was also security for the cash instalments representing payment of the purchase price and outlined in the Promissory Note.

[14] As part of the Transaction, Vegherb also entered into subordination agreements with First West Credit Union ("FWCU") and Contech and with HSBC and Contech whereby Vegherb subordinated its interests in the personal property of the Company to those of HSBC and FWCU.

[15] In order to finance its several acquisitions Contech took on additional debt.

[16] Contech has faced significant challenges to its traditional business model moving from a distribution model to also include direct-to-consumer sales which added additional and unexpected costs to the acquisitions.

[17] Contech's business is also highly seasonal.

[18] Contech sustained aggregate losses of approximately $4.5 million over the last three fiscal years.

[19] Throughout 2014, Contech made numerous attempts to refinance its business with several institutional lenders, including asset-based lenders and other speciality financiers. One of the speciality financiers approached by Contech was Siena Lending Group LLC ("Siena"), which is the "Funder" under the Proposal.

[20] In or around early November 2014, Contech and Siena had reached an agreement on refinancing terms. Ultimately, however, the refinancing transaction did not complete due to difficulties Contech was experiencing with some of its creditors and suppliers including, but not limited to, Vegherb which refused to subordinate its security interest in Contech's assets to the security interest of Siena.

[21] Once it became clear the refinancing with Siena was not going to complete, Contech concluded that it had no viable options other than a formal restructuring as it does not have the funds needed to service its debt, pay its suppliers and continue to operate its business.

The Proposal

[22] On December 23, 2014, Contech filed the Proposal with the Trustee and the Office of the Superintendent of Bankruptcy (the "OSB"). Between December 23 and 24, 2014, the Trustee sent to all Affected Creditors:

a) a Notice of Proposal to Creditors dated December 23, 2014, whereby the Trustee provided all creditors with notice of the creditors' meeting to vote on the Proposal (the "Meeting");

b) a copy of the Proposal; and

c) a copy of the Trustee's First Report.

[23] Certain secured creditors of Contech are not affected by the Proposal, including Business Development Bank of Canada, HSBC, FWCU and Contech's equipment lenders. This is because the Trustee has determined that in a liquidation scenario they would be likely able to recover the debt owed to them, although this is not certain.

[24] Those creditors who the Trustee has estimated would not recover if Contech went bankrupt and its assets were liquidated are described in the Proposal as Affected Creditors.

[25] The Trustee values Contech's assets at $2,369,000.00, with an approximate liquidation value of $1.5 million. The Trustee does not expect the security to be sufficient to satisfy any liabilities subordinate to FWCU.

[26] In the Proposal the Affected Creditors are divided into classes of Affected Secured Creditors, Unsecured Creditors (some of whom are either Convenience Creditors or Equity Election Creditors), and Key Supplier.

[27] Adopting the terms as defined in s. 1.1 of the Proposal, it provides that:

a) All Affected Secured Creditors will receive one Common Share of Contech for every $0.08 of their Proven Claim.

b) All Unsecured Creditors with Proven Claims of $1,500 or less, or who elect to reduce their Proven Claim to that amount, ("Convenience Creditors"), will be paid in full.

c) Unsecured Creditors with Proven Claims greater or equal to $30,000 may elect to be treated as "Equity Election Creditors" and receive Common Shares of Contech at the rate of one Common Share for every $0.12 of their Proven Claim.

d) All other Unsecured Creditors (i.e. those with Proven Claims exceeding $1,500 who do not make one of the aforementioned elections) will receive $0.30 for every dollar of their Proven Claim.

[28] The Trustee and Contech take the position that Vegherb is in the class of Affected Creditors known as Affected Secured Creditors. All creditors in that class have general security agreements over Contech's personal property.

[29] Under the Proposal, the cash distributions to the Unsecured Creditors (other than the Key Supplier, as discussed below) shall be completed within 180 days of the Effective Date, and the distribution of Common Shares under the Proposal shall be completed within 14 days of the Effective Date. The Effective Date is the date when all conditions precedent to the Proposal have been satisfied.

[30] Under the Proposal, the Key Supplier is to receive $0.70 for every dollar of its Proven Claim over a longer period of time, provided that it first agrees with Contech to continue to supply product to Contech on terms acceptable to Contech.

[31] The Key Supplier voted in favour of the Proposal and has agreed to continue to supply product to Contech on cash-on-shipment payment terms, which is acceptable to the Contech.

[32] The reason that the Key Supplier is receiving additional recovery under the Proposal is that Contech considers that it is a critical supplier. The product the Key Supplier supplies accounts for approximately 25% of Contech's annual sales. If the

Key Supplier refused to continue to supply products to Contech, it is unlikely Contech could continue to carry on business. The result of this would be that the Proposal would fail, Contech would be deemed to be assigned into bankruptcy and the Affected Creditors would not recover any part of their Proven Claims.

[33] The Meeting was held on January 8, 2015. At the Meeting, a large majority of Affected Creditors voted in favour of the Proposal as follows:

a) In the Unsecured Creditor Class, the Proposal was approved by 96% in number of the voting Unsecured Creditors holding 99% of the Proven Claims of the voting Unsecured Creditors

b) In the Affected Secured Creditor Class, the Proposal was approved by 96% in number of the voting Affected Secured Creditors holding 76% of the Proven Claims of the voting Affected Secured Creditors.

[34] Only one Affected Secured Creditor – Vegherb – did not vote in favour of the Proposal.

License Agreement

[35] A central issue on this application is whether or not a License Agreement between Contech and Vegherb is a “security agreement” within the meaning of the *Personal Property Security Act*, R.S.B.C. 1996, c. 359, s. 1(1) [*PPSA*], meaning an agreement that creates or provides for a security interest.

[36] This question requires analysis of the applicable provisions of the *PPSA*, the law interpreting those provisions, and the substance of the License Agreement.

[37] The License Agreement can only be understood in the commercial context of the entire transaction between Contech and Vegherb.

[38] In its terms the License Agreement makes reference to an Asset Purchase Agreement and Promissory Note and an Assignment Agreement and so it is important to understand these aspects of the transaction.

Asset Purchase Agreement

[39] By the Asset Purchase Agreement (the "APA"), Contech agreed to purchase the Vegherb "Purchased Assets" for a purchase price of $4,438,750 US. The purchase price was payable in part by cash of $857,100 immediately, which was paid; the issuance of 4 million Contech shares to Vegherb, valued at $.032 per share (in other words, approximately $1.28 million of the purchase price was paid in shares, which have been issued); and the remaining amount of $2,301,650 was payable in instalments and secured by the Promissory Note.

[40] Of the installment payments due under the APA and Promissory Note, there were three installments to be paid by Contech to Vegherb by April 1, 2014, namely $551,650 plus $50,000 plus $200,000 for a total of $801,650. I understand that Contech made these payments.

[41] After that Contech was to pay an annual installment of $300,000 by October each year, beginning in 2014, for a total of five payments ending in October 2018 i.e. for a total of $1.5 million. These figures seemed to be based on Contech's expected "Garden Sales" of $4 million each fiscal year.

[42] Contech did not pay the $300,000 instalment to Vegherb by October 31, 2014. The APA provided at article 3.10 that if Contech failed to pay an installment payment when due and that failure continued for five business days, all of the remaining portions of the purchase price as evidenced by the Promissory Note would become immediately due and payable.

[43] Contech attempted to cure the missed payment by delivering payment to Vegherb of the $300,000. The evidence states this was "on or around November 6, 2014", but in any event Vegherb's position is that it was outside of the five day cure period.

[44] The delivery of the payment to Vegherb was seen by other creditors as in breach of Vegherb's subordination agreements and ultimately the payment was returned to Contech.

[45] In summary, approximately $1.5 million US principal remains outstanding to Vegherb on account of the $4.438 million purchase price of the assets, of which only $300,000 would have been due had Vegherb not defaulted. With interest and exchange, Vegherb's position is that its claim under the Proposal is $1,712,358.34 CA.

[46] I come back to the structure of the Vegherb deal. What the parties did was carve the Vegherb IP out of the definition of assets in the APA and instead deal with it by way of two agreements: the License Agreement and Assignment Agreement.

[47] The Purchased Assets were defined in the APA as all the assets of Vegherb excluding the Vegherb IP. The allocation of the purchase price was primarily to: inventory, in the approximate amount of $1.1 million; and to "goodwill and other intangibles" in the approximate amount of $3.8 million. There were some other assets and a deduction for accounts payable as well.

[48] Despite the APA purporting to exclude the IP from the assets being sold under it, Vegherb gave representations and warranties under the APA as to the whole of its IP and the validity of its title to the IP, which was listed on Schedule C.

[49] Also, the principal of Vegherb, Mr. Anthony Topping, admits that the value assigned in the APA to the "goodwill and other intangibles" included the value of the right to use the IP and to acquire the IP.

[50] As mentioned, the IP was dealt with by a License Agreement and Assignment Agreement.

License Agreement

[51] The License Agreement included the following terms:

> **BACKGROUND**
>
> A. The Licensor and the Licensee have entered into an asset purchase agreement as of the date hereof (the "APA") pursuant to which the Licensee is to purchase the Purchased Assets (as defined in the APA) and is to license the Intellectual Property (as defined in the APA), in each case from the Licensor; and

B. The Licensor has agreed to grant to the Licensee an exclusive license to use the Intellectual Property worldwide on the terms and conditions set out herein,

...

2. LICENSE

2.1 In exchange for $1.00 and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged by the Licensor, the Licensor hereby grants to the Licensee the right and license under any and all of the Intellectual Property during the term of this Agreement to use, disclose, reproduce, publish, publicly perform, publicly display, develop, make, have made, sell, offer for sale, advertise, market, distribute, supply, import, use, adapt, prepare derivative works of and otherwise exploit the Intellectual Property. The Licensor expressly grants to the Licensee the right to sublicense to one or more wholly-owned subsidiaries of the Licensor, any and all of the rights licensed to the Licensee pursuant to this Agreement.

3. TERM AND TERMINATION

3.1 The term of this Agreement commences on the date hereof and will terminate on the earlier of:

3.1.1 the Licensee fulfilling its obligations in favour of the Licensor with respect to the payments evidenced by the Promissory Note dated of even date herewith and delivered at Closing pursuant to the APA (the “Payments”); or

3.1.2 the Licensee defaulting on its obligations in favour of the Licensor to make the Payments.

3.2. Effect of Termination

3.2.1. Upon the termination of this Agreement in accordance with Section 3.1.1, the Licensor shall transfer to the Licensee the Intellectual Property pursuant to the terms of an Assignment Agreement of even date herewith.

3.2.2. Upon the termination of this Agreement in accordance with Section 3.1.2, the Licensee may continue to exercise the rights granted to it under Section 2.1 in connection with any products made in conjunction with the Intellectual Property that have been manufactured, included in work in process or are called for pursuant to contracts or purchase orders from existing customers of the Licensee as of the date of such termination.

[52] As is seen and I have already noted, the License Agreement made reference to the APA, the Promissory Note payments, and the Assignment Agreement. In short, if all of the Promissory Note payments were made, the License Agreement was meant to terminate and Contech would automatically acquire title to the IP by operation of the Assignment Agreement.

The Assignment Agreement

[53] The Assignment Agreement referred to in the License Agreement was between Contech, defined as the Company, and Vegherb, defined as the Assignor. It provided at article 1 that:

> **Assignment.** Subject to the Promissory Note Payments having been received by the Assignor or its permitted successor or assign, for $1.00 and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged by the Assignor, the Assignor hereby assigns, sells and transfers to the Company, for the Company's benefit and the benefit of its successors and assigns, all of the Assignor's rights, title and interest in and to the Intellectual Property, including, without limitation, all common law rights and the goodwill associated with the Intellectual Property throughout all countries and jurisdictions, including all applications and registrations in respect thereof, and the right to file further applications for the Intellectual Property and to receive registrations therefor.

[54] I turn now to the applicable provisions of the *PPSA* in considering whether or not the License Agreement is a security agreement.

The *PPSA*

[55] Subsection 2(1) of the *PPSA* provides:

> 2(1) Subject to section 4, this Act applies
>
> (a) to every transaction that in substance creates a security interest, without regard to its form and without regard to the person who has title to the collateral, and
>
> (b) without limiting paragraph (a), to a chattel mortgage, a conditional sale, a floating charge, a pledge, a trust indenture, a trust receipt, an assignment, a consignment, a lease, a trust, and a transfer of chattel paper if they secure payment or performance of an obligation.
>
> [Emphasis added.]

[56] Section 1 of the *PPSA* includes the following definitions:

> "security agreement" means an agreement that creates or provides for a security interest and, if the context permits, includes
>
> (a) an agreement that provides for a prior security interest, and
>
> (b) writing that evidences a security agreement;
>
> "security interest" means
>
> (a) an interest in goods, chattel paper, investment property, a document of title, an instrument, money or an intangible that secures payment or

> performance of an obligation, but does not include the interest of a seller who has shipped goods to a buyer under a negotiable bill of lading or its equivalent to the order of the seller or to the order of an agent of the seller, unless the parties have otherwise evidenced an intention to create or provide for a security interest in the goods, and….

[57] The exclusions in s. 4 of the *PPSA* are not relevant in this case.

[58] The words of s. 2(1)(a) of the *PPSA* make it clear that question of whether or not a transaction created a security interest is determined by the substance of the transaction, not the form. An example of such a transaction includes a conditional sale securing payment or performance of an obligation, as set out in s. 2(1)(b).

Authorities Interpreting the *PPSA*

[59] Both the title and form of a transaction are unimportant in determining whether a transaction is a security agreement; what is important is the substance of the transaction: s. 2(1), *PPSA*; *Anderson's Engineering Ltd. (Re) (Trustee of)*, 2001 BCSC 1476 at para. 85 [*Anderson's Engineering*].

[60] In looking at the substance of the transaction, the court will consider "the purpose of the transactions; the role and relationship of the parties; the practicality and commercial reality; and the intention of the parties with respect to the transactions", as held in *Manning Jamison Ltd. v. Registrar of Travel Services*, 1999 BCCA 185 at para. 26.

[61] The interplay of s. 2(1) and (2) are such that it is only logical that if the substance of an agreement is sufficiently akin to one of the enumerated transactions in s. 2(2), then the agreement will create a security interest and be a security agreement.

[62] To this effect the Court in *Anderson's Engineering* held at para. 84:

> If a conditional sale (an agreement by which a seller retains title to goods until the buyer pays the full price for the goods) is specifically included in the scope of the *Personal Property Security Act*, a mechanism that is alleged to accomplish exactly the same thing by the retention of title documents, in

> substance, also creates a security interest and is included in the scope of the *Personal Property Security Act*.

[63] The Court in *Anderson's Engineering* cited with approval the case of *Haibeck v. No. 40 Taurus Ventures Ltd*. (1991), 59 B.C.L.R. (2d) 229 (B.C.S.C.) [*Haibeck*].

[64] *Haibeck* involved a contest in priorities as between the charge created by a debenture and a conditional sales contract in relation to appliances installed in the subject condominium project. There had been default under both instruments, and the petitioner was also seeking an order cancelling the claim of the seller of the appliances to the appliances.

[65] The conditional sales contract in *Haibeck* expressly stated that title to the goods would remain in the seller until there was payment in full. The seller also had the right under the contract to pay off any claims against the goods, such as liens. The Court noted the concern that the seller stood to lose the appliances without monetary consideration if the conclusion was reached that the *PPSA* applied to the contract, stating that the equities favoured the seller: at 235.

[66] Despite all of the above factors, the Court in *Haibeck* had no hesitation in concluding that the conditional sales contract was a "security agreement" creating a "security interest": at 235. The fact that the purchaser had not paid for the appliances, and that under the contract the seller retained title, was irrelevant.

Analysis of the Substance of the License Agreement

[67] Turning to an analysis of the License Agreement at issue, as the above referenced law makes clear, it is necessary to look at the substance of the transaction in question, in the context of its commercial purpose and the relationship of the parties.

[68] The purpose of the transactions between Vegherb and Contech, and the relationship of these parties, in a commercial context, are readily apparent from a review of the agreements of these parties. While principals of each have filed

affidavits stating what their intentions were, my impression was that this evidence was self-serving argument and I did not find it to be determinative.

[69] I have no difficulty in concluding that the License Agreement was in substance similar to a conditional sales agreement for the sale of all of the IP, by providing that Vegherb would temporarily retain title to the IP merely as a means to secure payment of the purchase price being paid for all of the assets.

[70] The License Agreement was not a means for Vegherb to keep ownership of the IP beyond the date of payment of the purchase price, nor was it a means for Vegherb to receive ongoing benefits in relation to that ownership. Payment by Contech to Vegherb under the License Agreement was not based on royalties for revenues earned by use of the IP; it was not based on any performance milestones to be met by Contech in using the IP; and there were no restrictions on Contech's use of the IP geographically or temporally.

[71] It was clear that the intention of the parties was for Vegherb to sell the IP to Contech as part of the sale of Vegherb assets to Contech. The only specific consideration mentioned under the Assignment Agreement for transfer of the IP, after the conditions of making the Promissory Note payments were met, was payment of $1 which had already been made. If that was the only value of the IP the parties would not be bringing these arguments to court. Clearly the value of the IP was part of the value attributed to "goodwill and other intangibles" which was part of the purchase price for the total assets of Vegherb.

[72] The structure of the entire transaction was that the purchase price of all of the assets of Vegherb, including the IP, was secured by Vegherb seeking to retain title of the IP until the entire payments due under the Promissory Note were paid.

[73] There were no other conditions under the License Agreement that had to be met by Contech in order to effect transfer of title to the IP from Vegherb to Contech other than payment of the installment payments secured by the Promissory Note in relation to the sale of the total asset package.

[74] Despite all of this, Vegherb argues that there were two aspects of the License Agreement that are particularly important in proving that it was a true license and not a conditional sales agreement.

[75] First, Vegherb points to Article 4.1 of the License Agreement. That is a clause dealing with unauthorized use or infringement of the IP by a third party. The clause gave Vegherb some rights to take action to prevent the unauthorized use or infringement.

[76] Article 4.1 of the License Agreement reads:

> THIRD PARTY INFRINGEMENT
>
> If either party becomes aware of any unauthorized use, misappropriation or infringement of the proprietary rights granted to Licensee under this Agreement, the party having such knowledge shall immediately give written notice of the details of the unauthorized use or infringement to the other party. Within 30 days of such notice, both parties shall confer to determine the course of action to be taken with respect to such unauthorized use or infringement. In the event Licensor does not take within 60 days of such notice all reasonable steps and actions necessary to prevent such unauthorized use or infringement from continuing, Licensee shall have the right to take such action as reasonably necessary and appropriate in its own name or the name of Licensor. The parties shall cooperate with each other to the extent reasonably necessary in any legal actions brought pursuant to this provision, including consulting with each other in the conduct of the proceedings as may effect their respective interests. Any damages and other amounts recovered in such proceeding shall be first applied to the reasonable costs and expenses incurred in prosecuting such actions, and any remaining amounts shall be payable to Licensee.

[77] I do not find Article 4.1 to support Vegherb's argument that the substance of the agreement was not a conditional sale agreement. There are several points about Article 4.1 that equally confirm Contech's position that the true substance of the agreement was a conditional sale agreement with each party to it having some kind of an interest in the IP:

a) the opening sentence of the clause recognizes that the agreement granted "proprietary rights" to Contech;

b) both parties were required to confer to determine the course of action if either one became aware of any unauthorized use or infringement of the IP;

c) in the event Vegherb failed to take steps to prevent the unauthorized use or infringement of the IP, Contech had the right to take such action as reasonably necessary and appropriate, either in its own name or in the name of Vegherb;

d) each were to cooperate with the other in any legal actions brought, including consulting with each other in the conduct of the proceedings as "may effect their respective interests";

e) any damages and other amounts recovered in such proceedings would first be applied to costs and expenses of prosecuting the action and any remaining amounts "shall be payable to" Contech.

[78] Similar language regarding the right of the seller to take action to protect property the subject of a conditional sale agreement can be found in some conditional sale agreements. For example, in the conditional sale agreement in *Haibeck* there was language allowing the seller to pay off any and all claims against the goods, including taxes, liens, charges and encumbrances, and requiring the buyer to notify the seller of any attachment or other judicial process affecting the goods.

[79] These types of clauses are entirely consistent with conditional sales agreements and are there to protect the seller only until the payment price is fully paid and the title to the property passes to the buyer.

[80] The other aspect of the License Agreement that Vegherb argues is significant in supporting its position that the true nature of the agreement is a license agreement, is the restriction in articles 2.1 and 6.5 of the Agreement which limited Contech's right to sublicense or assign the license to only a "wholly-owned subsidiary" without Vegherb's consent.

[81] However, I do not find these provisions any more indicative of a license agreement than a conditional sales agreement. These restrictions on assignment or sublicensing were simply consistent with Vegherb's goal under the agreement to retain title to the IP until the purchase price was paid, after which these restrictions would terminate and Contech would have the ability to do whatever it wanted with the IP.

[82] These were not true restrictions on the ability to use the IP within Contech's business, which was unlimited.

[83] The question of whether or not the License Agreement is a security agreement in the nature of a conditional sale agreement brings to mind the "duck test". The License Agreement looks like a conditional sales agreement meant to secure the payment of the purchase price and acts like it.

[84] There is no business purpose for the License Agreement other than to function as a form of security for Vegherb to secure the payment of the purchase price on the sale of the total package of Vegherb assets, and once the purchase price payments under the Promissory Note were paid in full, the title to the IP would pass to Contech.

[85] The description of the document as a "license agreement" does not change what it is in substance. I find that it is a security agreement creating a security interest under the *PPSA*.

Implications if the License Agreement is a Security Agreement

[86] What then follows, if the License Agreement is a security agreement within the meaning of the *PPSA*?

[87] Both Vegherb and Contech had some proprietary interests in the IP under the License Agreement until the purchase price for Vegherb's assets was paid in full: Vegherb held title to the IP subject to Contech's rights, and Contech had the right to

use the IP and to obtain title to the IP upon final payment of the purchase price in accordance with the Promissory Note.

[88] Contech's intangible rights in respect of the IP formed part of its basket of assets. Thus, creditors with general security agreements attaching to the whole of Contech's personal property, had security interests attached to Contech's proprietary rights with respect to the IP.

[89] This is made clear by the analysis in *Haibeck*. There the Court emphasized that no payment had been made under the conditional sale contract. The terms of the contract provided that title remained with the seller. Despite this, the purchaser-debtor was found to have rights to the property in question.

[90] The Court in *Haibeck* at 240 cited the logic in *Euroclean Canada Inc. v. Forest Glade Investments Ltd. et al.* (1985), 49 O.R. (2d) 769 (C.A.) at 18 per Houlden J.A. as follows:

> By the conditional sales agreement, Brazier [the conditional purchaser] acquired the right to immediate possession of the equipment and the right to receive legal title upon payment of the full purchase price. I hold that those rights were sufficient for Mady's (debenture holder) security interest to attach.

[91] The License Agreement provided an extra form of security to Vegherb (which also had a general security agreement). However, because it fits within the definition of security agreement under the *PPSA*, once there is a contest amongst secured creditors, Vegherb's rights under the License Agreement as between it and other secured creditors are treated just like other security interests under the *PPSA*.

[92] This means that in a bankruptcy of Contech, Vegherb's secured claim in relation to the IP will be subject to the priorities of other secured creditors; and any realization of Contech's assets for the benefit of creditors will include realization of Contech's rights to the IP. The Trustee has already concluded that Vegherb would recover nothing in the event of a bankruptcy, after liquidation of Contech's assets.

[93] Likewise, short of bankruptcy, in a proposal under the *BIA*, Contech's rights in relation to the IP form part of its basket of assets.

[94] The specific terms of the Proposal in question address what happens if the Proposal is implemented.

[95] The Proposal has terms providing for extinguishment of claims of creditors upon implementation of the Proposal, as set out in section 2.4 of the Proposal.

[96] With respect to Affected Secured Creditors, Section 2.4 provides that upon the conversion date and subject to Contech meeting its obligations to creditors under the Proposal, all Affected Secured Creditors will release Contech and its directors and officers from all claims that arose before the filing date regardless of the date of crystallization of such claims.

[97] Claims are defined in the Proposal as:

> …any right or claim of any person against [Contech]…including any indebtedness, liability or obligation owed to such person as a result of any…right of ownership or title to, or to a trust or deemed trust against, any of the property or assets of the [Contech], whether or not such right or claim is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, unsecured, perfected, unperfected, present, future, known, or unknown….
>
> [Emphasis added.]

[98] The Proposal definition of "Affected Secured Creditor" includes those creditors having a Security Interest in any assets of the Company which ranks in priority subordinate to the Security Interest of FWCU, and includes Vegherb.

[99] I agree with Contech that the natural result of the Court's conclusion that the License Agreement is a security agreement under the *PPSA* means that now that Contech is under the umbrella of the *BIA*, Contech's rights in the IP are part of its basket of assets; and Vegherb's claim to title of the IP is simply a secured claim which can be extinguished by operation of the *BIA* just like what can happen to other secured claims against Contech's property. Once Vegherb's claim is extinguished

then the property in the IP will reside entirely in Contech subject to any secured interests of other parties that have not been released.

Termination of the License Agreement

[100] Vegherb argues that the fact that Contech defaulted in payment caused automatic termination of the License Agreement pursuant to its own terms; this termination was confirmed by Vegherb by letter from its counsel to Contech on October 31, 2014. Vegherb's letter demanded that Contech cease and desist from using the IP.

[101] Vegherb's argument seems to be if at one time the Licence Agreement might have been a security agreement (which it denies), at a minimum it was no longer such by the date of the Proposal on December 23, 2014.

[102] It is to be noted that there was no evidence that Contech agreed to Vegherb's position that the License Agreement was terminated due to default or that Contech no longer had any rights to the IP. There is no evidence that Contech ceased to use the IP by that date.

[103] One wonders what would have happened had Contech agreed with Vegherb's position: would it be subject to claims being brought by other creditors that it had given Vegherb a fraudulent preference?

[104] I cannot accept Vegherb's argument that because of either the default in payment or Vegherb's unilateral notice of termination, all of Contech's rights to the IP would then be taken out from under the umbrella of the *PPSA* and *BIA*. That argument suggests that Vegherb could unilaterally "opt-out" of the legislation governing security interests, the *PPSA*, and thereby take priority over an asset of the debtor for itself despite competing creditors. This would undermine one of the important purposes of the *PPSA*, which is to provide certainty amongst competing creditors as to how their interests in personal property will be ranked.

[105] The potential default of the debtor was the very reason for the security agreement which took the form of the License Agreement, and the very reason it is to be governed by the *PPSA*, rather than by terms which seek to give preference to Vegherb to these assets as against other creditors.

[106] Vegherb relies on the case of *DaimlerChrysler Financial Services (debis) Canada Inc. v. Mega Pets Ltd*., 2002 BCCA 242 [*DaimlerChrsyler*], which considered the effect of the *PPSA* in relation to competing claims by Canada Customs & Revenue Agency ("CRA"). The CRA claims were based on the *Income Tax Act* and the *PPSA* did not apply.

[107] Vegherb relies on the following passage in *DaimlerChrysler* at para. 8.

> There is no doubt that the purpose of the *PPSA* was to simplify the thicket of statutory and common law rules that previously governed various forms of chattel security, including chattel mortgages, leases, debentures and conditional sale agreements. Thus Professors Cuming and Wood stated in their *British Columbia Personal Property Security Act Handbook* (4th ed., 1998):
>
> > Section 2 and the definition of "security interest" in s. 1(1) give very few clues as to the nature of a security interest. It is clear that the locus of title to the collateral and the form of the transaction are not to be relied upon in determining whether or not a security interest exists. A security interest is proprietary in nature in that a secured party who has a valid security interest is not treated as an unsecured creditor. However, the Act avoids saying anything that allows the analyst to easily put security interests in one of the traditional categories of proprietary interest.
> >
> > A brief examination of the history of the Act reveals why this is so. The goal of the drafters was to merge separate streams of personal property security law into a single system. In this respect their goal was principally a pragmatic one; conceptualization, at least in traditional terms, was not important. Indeed, it was to be avoided. What was common to the forms of transactions that where the focus of attention of the drafters was that they all had essentially had the same function: to provide through a contract to a person to whom an obligation was owed an interest in personal property that would permit that person to look to the property as a source of compensation should the obligation not be performed. The effect of the transaction, not its form or the way in which the interest arose, was to be determinative.
> >
> > There is no need to be concerned about the juridical nature of the security interest so long as the issue being addressed is one that falls

> within the scope of a statutory regime designed to regulate security interests. Once the conclusion is reached that a security interest is involved, further inquiry as to the essential characteristics of that interest is not required. However, the same approach cannot be used outside the regime. For example, the holder of a security interest might find himself in a legal competition in which the outcome will depend upon the nature of the interest held by each of the competitors. In this context it may not be good enough to conclude that the secured party has an interest in the collateral. It may be necessary to determine the nature and extent of that interest. [at 31-2; emphasis added in *DaimlerChrysler*.]

[108] I do not see the case of *DaimlerChrysler* as assisting Vegherb.

[109] The Court in *DaimlerChrysler* recognized that the purchaser of the car under the conditional sale agreement, where all payments had not yet been made, had some kind of a property interest in the car despite not having title to it. Madam Justice Newbury noted at para. 32 that a conditional purchaser "acquires a property interest in the chattel over time, reflecting his or her increasing 'equity'."

[110] However, because the *PPSA* did not apply, the Court in *DaimlerChrysler* found that the vehicle was not the property of the co-purchasers who were required to pay all amounts owing under the agreement before title would pass: at para. 40. The Court's judgment expressly noted that this would be a different result if the *PPSA* applied, holding at para. 41:

> [41] Of course, the distinction between conditional sale agreements and other forms of chattel security was effectively eliminated for purposes of the *PPSA* — as Cuming and Wood noted in their handbook, *supra* (see para. 8 above), one of the goals of the legislation was to ensure that the "juridical nature of the security interest" was secondary to the registration regime. This is the lesson of the cases cited by the trial judge at para. 33 of her Reasons: *Haibeck v. No. 40 Taurus Ventures Ltd., supra, Euroclean Canada Inc. v. Forest Glade Investments Ltd., supra*, and *Re Ottaway* (1980) 110 D.L.R. (3d) 231 (B.C.C.A.). But as Cuming and Wood also note, the same approach cannot be used outside the *PPSA* regime. The particular terms of the agreement in question, such as that reserving title in the conditional seller, remain valid and must be considered.
>
> [Emphasis added.]

[111] To be sure *DaimlerChrysler* recognized that agreements deemed to be security agreements for purposes of the *PPSA* will nonetheless be considered on

their terms alone and without reference to the *PPSA* in the context of proceedings that have nothing to do with the *PPSA*. Contech does not argue otherwise. But this is not such a proceeding.

[112] This proceeding has everything to do with competing interests of creditors, secured and unsecured.

[113] The *BIA* and *PPSA* work in a complimentary fashion as was seen by the Supreme Court of Canada's analysis in *Giffen (Re),* [1998] 1 S.C.R. 91. That case dealt with a lease of car to a person who went into bankruptcy. The lessor had not registered a financing statement under the *PPSA* in respect of the lease. The question was whether this meant, pursuant to s. 20(b)(i) of the *PPSA*, that the lessors' interest in the car was of no effect as against the trustee in bankruptcy. The trial judge answered the question in the affirmative, but was overturned by the Court of Appeal which held that the property belonged to the lessor.

[114] On appeal to the Supreme Court of Canada in *Giffen (Re)*, the appeal result was overturned. The Court held at paras. 25-26:

> **25** At the outset, it is important to note that the Court of Appeal's holding in the present appeal rests on the principle that the "property of the bankrupt" shall vest in the trustee (s. 71(2) *BIA*) and that only the property of the bankrupt shall be distributed among the bankrupt's creditors (s. 67(1) *BIA*). In the opinion of the Court of Appeal, the bankrupt, as lessee, did not have a proprietary interest in the car, and since the trustee obtains its entitlements to the contents of the bankrupt's estate through the bankrupt, the trustee cannot assert a proprietary interest in the car. In my view, the Court of Appeal, with respect, erred fundamentally in focussing on the locus of title and in holding that the lessor's common law ownership interest prevailed despite the clear meaning of s. 20(b)(i).
>
> **26** The Court of Appeal did not recognize that the provincial legislature, in enacting the *PPSA*, has set aside the traditional concepts of title and ownership to a certain extent. T. M. Buckwold and R. C. C. Cuming, in their article "The Personal Property Security Act and the Bankruptcy and Insolvency Act: Two Solitudes or Complementary Systems?" (1997), 12 Banking & Finance L. Rev. 467, at pp. 469-70, underline the fact that provincial legislatures, in enacting personal property security regimes, have redefined traditional concepts of rights in property:
>
> > Simply put, the property rights of persons subject to provincial legislation are what the legislature determines them to be. While a

> statutory definition of rights may incorporate common law concepts in whole or in part, it is open to the legislature to redefine or revise those concepts as may be required to meet the objectives of its legislation. This was done in the provincial *PPSA*s, which implement a new conceptual approach to the definition and assertion of rights in and to personal property falling within their scope. The priority and realization provisions of the Acts revolve around the central statutory concept of "security interest". The rights of parties to a transaction that creates a security interest are explicitly not dependent upon either the form of the transaction or upon traditional questions of title. Rather, they are defined by the Act itself.
>
> [Emphasis added.]

[115] The Supreme Court of Canada in *Giffen (Re)* noted that the lease was a "security interest" under the *PPSA*. This security interest could be asserted against the lessee and a third party claiming a right in the car. However, as explained at paras. 32-34, as a security interest, it was subject to both the *PPSA* and *BIA*, as follows:

> However, the lessor's security interest remained vulnerable to the claims of third parties who obtain an interest in the car through the lessee including, trustees in bankruptcy. In order to protect its security interest from such claims, the lessor must therefore perfect its interest through registration of its interest (s. 25), or repossession of the collateral (s. 24). The lessor did not have possession of the car, and it did not register its security interest. Thus, prior to the bankruptcy, the lessor held an unperfected security interest in the car. This brings us to the *BIA*.
>
> D. *The Bankrupt's Interest in the Car Vests in the Trustee*
>
> **33** Section 71(2) of the *BIA* provides that, upon an assignment into bankruptcy, the bankrupt's "property . . . shall, subject to this Act and to the rights of secured creditors, forthwith pass to and vest in the trustee". Section 2 of the *BIA* defines "property" very broadly to include "every description of estate, interest and profit, present or future, vested or contingent, in, arising out of or incident to property".
>
> **34** In my opinion, the bankrupt's right to use and possession of the car constitutes "property" for the purposes of the *BIA* and the trustee, by virtue of s. 71(2) of the *BIA*, succeeds to this proprietary right.

[116] Thus in *Giffen (Re)* the Supreme Court of Canada explained that the lessee had a proprietary interest to the car under both the *PPSA* and *BIA*: at para. 37.

[117] The comments in *Haibeck* are to the same effect, citing at page 234 the same handbook of Cumming and Wood as was relied on in *DaimlerChrysler*:

> The substance test of section 2 [of the *PPSA*] ignores both title and form as factors in characterizing transactions. If a transaction is one under which a party gives or recognizes that someone else has an interest in his or her property in order to secure payment or performance of an obligation, it is a security agreement. A conditional sales contract generally provides that the title and property in the goods sold remains in the seller until the entire purchase price is paid. Nevertheless, since under section 2 the retention of title and property is irrelevant, this type of an agreement is treated under the Act as being one in which property in the goods vests in the buyer subject to the seller's security interest. Substance rather than form is the central consideration. [Emphasis in Original.]

[118] The same analysis applies here. I find that by the License Agreement, Contech acquired the proprietary right to immediate use of the IP and the right to receive legal title upon payment of the remaining debt, the full purchase price. This is part of Contech's personal property to which claims of secured creditors of Contech attached (that is, those creditors who registered security interests against all of Contech's personal property). Mere default by Contech does simply result in that property becoming the sole property of Vegherb.

Declaratory Relief

[119] Contech seeks a declaration in respect of the IP that it says will provide certainty to all other parties interested in knowing Contech's asset picture following the Proposal, and to allow Contech the ability to take any necessary steps to maintain and protect the IP and to register the IP in its name. I have already made findings that support Contech's position.

[120] It is clear that courts in bankruptcy matters have discretion to make prospective declarations. Obviously one ought to be careful in doing so. Here, the issue has now been fully canvassed as between Contech and Vegherb and it is important to avoid having this issue re-litigated after the Proposal. A declaration addressing the status of the IP on implementation of the Proposal will assist in providing certainty not only to the debtor but to all creditors and any parties re-financing Contech.

[121] However I am not certain that I accept Contech's revised wording submitted on the application before me.

[122] It strikes me that the wording of any declaration should mirror that of the Proposal. The Proposal states at s. 2.4 that upon the conversion date and subject to Contech meeting its obligations to creditors under the Proposal, all Affected Secured Creditors shall release Contech and its directors and officers from all claims that arose before the filing date regardless of the date of crystallization of such claims.

[123] I conclude that Contech is entitled to such a declaration as well as further a supplemental language to make it more precise and clear that upon the implementation of the Proposal including Vegherb receiving the Contech shares, Vegherb's rights to the IP will be extinguished and Contech will be permitted to take all necessary steps to register the IP in Contech's name.

Review of the Proposal

[124] I turn now to the application for approval of the Proposal.

[125] The trustee applies for approval of the Proposal pursuant to s. 55 of the *BIA*. The court may refuse to approve pursuant to s. 59(2) if of the opinion "the terms of the proposal are not reasonable or are not calculated to benefit the general body of creditors".

[126] The parties agree that the leading authorities such as *Kitchener Frame Ltd. (Re)*, 2012 ONSC 234 [*Kitchener Frame*] at para. 19 and *Magnus One Energy Corp. (Re)*, 2009 ABQB 200 [*Magnus One*], at para. 10, establish that before it can approve a proposal the Court must be satisfied that:

a) the terms of the proposal are reasonable;

b) the terms are calculated to benefit the general body of creditors; and

c) the proposal is made in good faith.

[127] In determining whether a proposal has met these branches of the test for approving a proposal, the Court should consider the payment terms of the proposal and whether the distributions provided for in the proposal are "adequate to meet the

requirements of commercial morality and maintaining the integrity of the bankruptcy system": *Kitchener Frame*, at para. 22; *Magnus* at para. 11.

[128] The Court is not bound to accept a proposal even if it is approved by creditors and recommended by a trustee: *Magnus* at para. 11.

[129] Contech submits that the Proposal represents the best offer Contech can make to its Affected Creditors while still retaining the support of Siena and ensuring that Contech has sufficient funds to carry on business going forward.

[130] Vegherb raises many issues with respect to the Proposal which I will address in turn.

Classification of Creditors

[131] One of Vegherb's strong objections to the form of the Proposal is the fact that it groups it into a class of Affected Secured Creditors. Vegherb asserts it should be in its own class as a secured creditor because the other creditors in its class are all debenture holders who always expected to ultimately receive equity in Contech. In contrast, Vegherb says that it is the seller of assets to Contech waiting to get paid for those assets.

[132] Section 50(1.4) and (1.5) of the *BIA* state:

> (1.4) Secured claims may be included in the same class if the interests or rights of the creditors holding those claims are sufficiently similar to give them a commonality of interest, taking into account
>
> (*a*) the nature of the debts giving rise to the claims;
>
> (*b*) the nature and rank of the security in respect of the claims;
>
> (*c*) the remedies available to the creditors in the absence of the proposal, and the extent to which the creditors would recover their claims by exercising those remedies;
>
> (*d*) the treatment of the claims under the proposal, and the extent to which the claims would be paid under the proposal; and
>
> (*e*) such further criteria, consistent with those set out in paragraphs (*a*) to (*d*), as are prescribed.
>
> (1.5) The court may, on application made at any time after a notice of intention or a proposal is filed, determine, in accordance with

> subsection (1.4), the classes of secured claims appropriate to a proposal, and the class into which any particular secured claim falls.

[133] In *Re Canadian Airlines Corp., Re* (2000), 19 C.B.R. (4th) 12 [*Canadian Airlines*] the Alberta Court of Queen's Bench considered classification issues. While that case dealt with the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, the approach is similar under the *BIA*. The Court held at paras. 14-19:

> **14** The starting point in determining classification is the statute under which the parties are operating and from which the court obtains its jurisdiction. The primary purpose of the C.C.A.A. is to facilitate the re-organization of insolvent companies, and this goal must be given proper consideration at every stage of the C.C.A.A. process, including classification of claims see for example, Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd. (1988), 72 C.B.R. (N.S.) 20 (Alta Q.B.)
>
> **15** Beyond identifying secured and unsecured classes the C.C.A.A. does not offer any guidance to the classification of claims. The process, instead, has developed in the case law.
>
> **16** A frequently cited description of the method of classification of creditors for the purposes or voting on a plan, under the C.C.A.A., is Sovereign Life Assurance Co. v. Dodd (1891) [1892] 2 Q.B. 573, (Eng. C.A.).
>
> **17** At page 583 (Q.B.), Bowen L.J. stated:
>
> > The word class is vague and to find out what is meant by it, we must look at the scope of the section which is a section enabling, the court to order a meeting of a class of creditors to be called. It seems plain that we must give such a meaning to the term 'class' as will prevent the section, being so worked as to result in confiscation and injustice, and that it must be confined to those persons, whose rights are not so dissimilar as to make it impossible for them to consult together with the view to their common interest.
>
> This test has been described as the "commonality of interest" test. All counsel agree that this is the test to apply to classification of claims under the C.C.A.A. However, there is a dispute on the types of interests that are to be considered in determining commonality.
>
> **18** Generally, the cases hold that classification is a fact-driven determination unique, to the circumstances of every case, upon which the court should be loathe to impose rules for universal application, particularly in light of the flexible, and remedial jurisdiction involved: see, for example, Re Fairview Industries Ltd. (1991) 11 C.B.R. (3d) 71 (N.S.T.D.)
>
> **19** The majority of the cases presented to me, held that commonality of the interest is to be determined by the rights the creditor has a vis-vis the debtor. Courts have also found it helpful to consider the context of the proposed plan and treatment of creditors under a liquidation scenario. In the absence of bad

> faith, motivation for supporting or rejecting a plan is not a classification issue in the authorities.

[134] Here the class of Affected Secured Creditors are those persons whose security ranks behind FWCU. They have a commonality of interest because they are unlikely to recover anything if Contech goes bankrupt. They all have general security agreements. Thus the rights of the members of this class vis-à-vis Contech are similar.

[135] The fact that Contech also has the License Agreement, as a form of a security agreement, in my view does not justify putting it in a different class. There is no evidence suggesting that the interest secured by that agreement ranks ahead of any of the interests secured by the general security agreements.

[136] I do not find it relevant that as debenture holders some of the persons in this class may have become debtors for different reasons than Vegherb became a debtor. As for the Proposal to provide shares, this does not favour debenture holders or disadvantage Vegherb. The fact is that Vegherb also was willing to become a shareholder of Contech as part of the payment of the purchase price for Vegherb's assets.

[137] I find that the classes of creditors determined in the Proposal are appropriate.

Abridgement of Time

[138] Vegherb also complains that the Trustee did not comply with the time requirements under s. 58(b) of *BIA* to give 15 days' notice to creditors of the court hearing to approve the Proposal.

[139] The Trustee and Contech have explained that the notice period was abridged due to the fact that the proposed financing to support the Proposal is based on a closing date of before January 31, 2015, and the financing is conditional upon court approval of the financing first.

[140] The Trustee reports that the OSB is aware and in agreement with the Trustee's decision to proceed despite the abridged notice period.

[141] It appears to me that the party objecting to the Proposal, Vegherb, has had notice and been able to fully advance its arguments opposing the proposal. I am not aware of any prejudice as a result of the abridged notice period and there appears to be a valid business reason for it. I am satisfied that the abridged notice period is appropriate given the urgent circumstances.

Related persons

[142] Vegherb also argues that certain persons who voted to approve the Proposal were "related" to Contech and so ought not to have voted, based on s. 54(3) of the *BIA*.

[143] "Related persons" are defined in s. 4 of the *BIA*.

[144] Vegherb's arguments were based on speculation.

[145] The Trustee and Contech have pointed to the Contech corporate chart attached at Appendix A to the Trustee's Report to Creditors and dispute that any persons who voted to approve the Proposal were related persons within the meaning of the *BIA*.

[146] The Trustee and Contech submit that to be related to a company, a person (or related group) must have control of that company. For the purposes of the *BIA* "control" of a company means *de jure* control, by which it is meant that they must own a majority of the voting shares of the company: *Re A. Zimet Ltd. and Woodbine Summit Ltd.* (1982), 44 C.B.R. (N.S.) 136 (Ont. Reg. in Bktcy), aff'd (1985), 56 C.B.R. (N.S.) 320 (Ont. Bktcy.), aff'd (1987), 64 C.B.R. (N.S.) 89 (Ont. C.A.).

[147] Notably, the *BIA* does not provide that management, shareholders, directors and officers of a company are, by virtue of being in such a position, related to that company: *Piikani Nation v. Piikani Energy Corp*., 2013 ABCA 293 at paras. 33-36.

[148] The Trustee and Contech submit that no Affected Creditor is "related" to Contech for the purposes of the *BIA* as no Affected Creditor has, or is part of a related group which has, *de jure* control over Contech. Many of the Affected Secured Creditors are also shareholders of the Company (and might have acquired additional shares but for the insolvency of the Company), but none have (or would have) sufficient shares to control the Company, whether alone or as part of a related group.

[149] I accept the submissions of the Trustee and Contech. There is no basis for concluding that persons voted in favour of the Proposal who were not entitled to vote.

Reasonableness of the Proposal

[150] As for the reasonableness of the Proposal itself, a key premise of Vegherb in its challenge to the Proposal, is that the Proposal is designed by its structure to "confiscate" the IP of Vegherb.

[151] Vegherb refers to the language of Farley J. in *Sammi Atlas Inc.*, *Re* (1998), 3 C.B.R. (4th) 171 (Ont. Ct. (Gen. Div.)) at para. 4 as follows:

> What of item 3 - is the Plan fair and reasonable? A Plan under the CCAA is a compromise; it cannot be expected to be perfect. It should be approved if it is fair, reasonable and equitable. Equitable treatment is not necessarily equal treatment. Equal treatment may be contrary to equitable treatment. One must look at the creditors as a whole (i.e. generally) and to the objecting creditors (specifically) and see if rights are compromised in an attempt to balance interests (and have the pain of the compromise equitably shared) as opposed to a confiscation of rights: see *Re Campeau Corp.* (1992), 10 C.B.R. (3d) 104 (Ont. Gen. Div.) at p. 109. It is recognized that the CCAA contemplates that a minority of creditors is bound by the Plan which a majority have approved - subject only to the court determining that the Plan is fair and reasonable: see *Northland* at p. 201; *Olympia & York* at p. 509.

[152] I do not accept that acquisition of the IP is a motive that underlies the structure of or making of the Proposal.

[153] The reason that the IP may be caught by the Proposal does not have to do with the structure of the Proposal but with the fact that the License Agreement is a

security agreement under the *PPSA* and with the fact that Contech is insolvent. A different proposal under the *BIA* would also capture the IP because of this.

[154] I find that the Proposal is designed as an attempt by Contech to restructure its debt and obtain new financing to enable it to continue its operations. If it is ultimately successful, under the Proposal the creditors affected by the Proposal will be better off than they would have been if Contech was simply to go bankrupt now.

[155] The fact that the Affected Creditors approve the Proposal by a large majority is a sign that they must have considered it fair and reasonable, and is entitled to considerable weight.

[156] Vegherb argues that the fact it is going to lose the IP without receiving ongoing payments for its use is unfair. Again, I do not agree that this is because of the structure of the Proposal. It is because of the terms of the License Agreement which is not a true license agreement.

[157] Vegherb complains that the structure of the Proposal essentially requires secured creditors to accept shares in Contech, not payment, in satisfaction of amounts owed. Vegherb argues that it may be subsequently difficult to redeem the shares since Contech is not publicly traded.

[158] I am not satisfied that the share component of the Proposal makes it unfair, and again I point to the fact that the majority of Affected Secured Creditors have voted in favour of it.

[159] It is interesting that under the proposed terms of refinancing, two persons are required to provide guarantees, including the President and CEO of Contech. This strikes me as an indication of the good faith that lies behind the Proposal.

[160] There is no suggestion that Contech has not provided full disclosure to its creditors of its assets and encumbrances against such assets. Vegherb argues that Contech did not disclose the dispute over the IP to creditors. However, that dispute

only gelled after the Proposal was filed and has evolved with Vegherb stating its position at the meeting of creditors.

[161] The Proposal is supported by the Trustee and there is no evidence to suggest that Contech has not acted in good faith or that its conduct is subject to any censure.

[162] Contech submits that the Proposal represents the best offer it can make to its Affected Creditors while still retaining the support of Siena and ensuring that Contech has sufficient funds to carry on business going forward.

[163] I am satisfied that the Proposal is fair and reasonable in respect of the whole body of Contech creditors, and meets the test for court approval.

Vegherb Application

[164] I will now address Vegherb's application.

[165] As mentioned, Vegherb seeks an order in the alternative that it be permitted to amend its proof of claim to change its position from that of a secured creditor to that of an unsecured creditor.

[166] Vegherb relies on s. 50.1(2) and s.132.1 of the *BIA*.

[167] Section 50.1 of the *BIA* states:

> 50.1 (1) Subject to subsections (2) to (4), a secured creditor to whom a proposal has been made in respect of a particular secured claim may respond to the proposal by filing with the trustee a proof of secured claim in the prescribed form, and may vote, on all questions relating to the proposal, in respect of that entire claim, and sections 124 to 126 apply, in so far as they are applicable, with such modifications as the circumstances require, to proofs of secured claim.
>
> (2) Where a proposal made to a secured creditor in respect of a claim includes a proposed assessed value of the security in respect of the claim, the secured creditor may file with the trustee a proof of secured claim in the prescribed form, and may vote as a secured creditor on all questions relating to the proposal in respect of an amount equal to the lesser of
>
> (a) the amount of the claim, and

> (b) the proposed assessed value of the security.
>
> (3) Where the proposed assessed value is less than the amount of the secured creditor's claim, the secured creditor may file with the trustee a proof of claim in the prescribed form, and may vote as an unsecured creditor on all questions relating to the proposal in respect of an amount equal to the difference between the amount of the claim and the proposed assessed value….
>
> [Emphasis added.]

[168] Section 132(1) of the *BIA* states in part:

> 132. (1) Where the trustee has not elected to acquire the security as provided in this Act, a creditor may at any time amend the valuation and proof on showing to the satisfaction of the trustee or the court that the valuation and proof were made in good faith on a mistaken estimate or that the security has diminished or increased in value since its previous valuation.
>
> (2) An amendment pursuant to subsection (1) shall be made at the cost of the creditor and on such terms as the court orders, unless the trustee allows the amendment without application to the court.

[169] Vegherb argues that the evidence establishes that its security is essentially valueless and therefore it ought to be considered an unsecured creditor.

[170] The problem with Vegherb's application is that it mischaracterizes the Proposal as including a proposed assessed value for its claim. The proposal did not do so. This means that s. 50.1(1) of the *BIA* applies to the Proposal but not ss. 50.1(2) and (3). Similarly, s. 132(1) of the *BIA* (allowing for amendments to valuations of security by a secured creditor) does not apply.

[171] In this regard I rely on the analysis of s. 50.1(1) set out in *Re WorkGroup Designs Inc.* (2008), 40 C.B.R. (5th) 1 (Ont. C.A.).

[172] Vegherb was entitled and did vote the full amount of its claim, as did other secured creditors

[173] Vegherb's application is therefore dismissed.

"The Honourable Madam Justice S. Griffin"