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October 23, 2018

**Tim Hill, Q.C.**
Boyne Clarke LLP
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Halifax Regional Municipality, NS B2Y 3Z5

**By Email and Facsimile:** **thill@boyneclarke.ca**
**(902) 463 7500**

Dear Mr. Hill:

**Re: Proposal of Burry's Shipyard Inc.**
**Our Client: Business Development Bank of Canada**
**Our File No. 30025378-00009**

In relation to the above noted matter, please find enclosed a copy of the Memorandum of Fact, Law and Argument of Business Development Bank of Canada and the Affidavit of Allison Philpott, the originals of which have been filed with the Court on today's date.

We trust the enclosed to be in order.

Yours Truly,

for Darren D. O'Keefe

DDO/at
Encl.

**Darren D. O'Keefe** | Partner
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**2018 01 22164**
**SUPREME COURT OF NEWFOUNDLAND AND LABRADOR**
**IN BANKRUPTCY AND INSOLVENCY**

**IN THE MATTER OF** the *Bankruptcy and Insolvency Act,* R.S.C. 1985, c. B-3, as Amended

**AND IN THE MATTER OF** the matter of the Proposal of Burry's Shipyard Inc.

**Estate No. 51-2397788**
**Court No. 22164**
**District: Newfoundland & Labrador**
**Division No. 01-Newfoundland & Labrador**

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# MEMORANDUM OF FACT, LAW, AND ARGUMENT OF BUSINESS DEVELOPMENT BANK OF CANADA

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# BUSINESS DEVELOPMENT BANK OF CANADA'S MEMORANDUM OF FACT, LAW AND ARGUMENT

Business Development Bank of Canada ("**BDC**") submits the following Memorandum of Fact, Law and Argument pursuant the Rule 57.30(2) of the *Rules of the Supreme Court, 1986,* as amended:

## PART I – MATERIAL FACTS

### *Relationship of the Parties and Filing of the Notice of Intention*

1. BDC is a senior secured creditor of Burry's Shipyard Inc. ("**BSI**") with current outstanding loans in the amount of $1,177,712.04 (the "cumulative loan balance"), which loans have been in arrears for periods varying from two (2) to four (4) months. Of the cumulative loan balance, one loan comprising 79% of it is four (4) months in arrears. Based on BSI's in-house Balance Sheet, BDC appears to hold over 70% of

BSI's issued and outstanding secured third party debt, with no third party lender owed more than $103,544.

2. On the 21st day of June, 2018, BSI, along with other related parties, entered into a forbearance agreement with BDC wherein BDC agreed to forbear on enforcing its debt, which was then in default, provided that BSI, along with other related parties, adhered to the terms of the Forbearance Agreement, including but not limited to the agreement to make monthly payments to BDC and comply with certain reporting requirements.

3. Following considerable time preparing the forbearance terms, within twenty (20) days after signing the Forbearance Agreement, on July 11, 2018, BSI filed a Notice of Intention to File a Proposal under Division I of the BIA (the "**NOI**").

4. From the date of signing the Forbearance Agreement to present, BSI has committed several defaults under the Forbearance Agreement, including but not limited to failure to pay amounts it had agreed to pay under the Forbearance Agreement and failure to receive a binding offer for the business and assets of BSI by September 30, 2018.

***Commencement of the Stay of Proceedings***

5. Following the filing of the NOI on July 11, 2018, and in accordance with the terms of the Forbearance Agreement, BSI, with the assistance of Deloitte Restructuring Inc. (the "**Proposal Trustee**"), was granted the opportunity to conduct a Sales and Investment Solicitation Process (the "**SISP**") to attempt to sell the business and assets of BSI, which SISP was initiated on June 28, 2018.

6. Since the commencement of the SISP, BSI and the Proposal Trustee have been unable to secure a binding offer for the purchase or re-finance of the business and assets of BSI.

***The First Extension of the Stay of Proceedings***

7. On August 2, 2018, BDC appeared before this Honourable Court where, as a result of the Proposal Trustee's recommendation, BSI sought an extension to the stay of proceedings under section 50.4(9) of the BIA, for a further period of 45 days, to continue with its

SISP and attempt to identify a viable purchaser for the business and assets of BSI. The extension was granted by Order of this Honourable Court. This extension therefore gave BSI up until September 21, 2018 to complete the SISP.

8. Between August 2, 2018 and September 21, 2018, BDC received updates on the SISP from the Proposal Trustee, but very little information regarding the likelihood of BSI to identify a purchaser and file a viable proposal. As a result of the lack of any binding offer being presented to BDC and due to BDC's growing concerns regarding the failure of the SISP and the impact the apparent failure would have on BDC's position, BDC wrote a letter to BSI on September 20, 2018 setting out its concerns. This letter was not acknowledged by BSI.

***The Second Extension to the Stay of Proceedings***

9. On September 21, 2018, BDC again appeared before this Honourable Court, at which time BSI sought another extension to the stay of proceedings under section 50.4(9) of the BIA for a further period of fourteen (14) days. At this hearing, BDC put its position on the record that given the unsuccessful SISP, the relatively weak expressions of interest received in the business and assets of BSI to date and the failure of BSI to provide even a draft proposal, the application to have the stay further extended should be dismissed.

10. Despite BDC's submissions on September 21, 2018, this Court granted the extension to the stay until October 5, 2018. BDC indicated on the record that it would continue to oppose any further extension to the stay if a viable purchase offer was not presented to BDC prior to the next comeback hearing on October 5, 2018.

11. Between September 21, 2018 and October 5, 2018, BDC's concerns continued to grow; as BSI did not demonstrate any reasonable progress in consummating a sale transaction pursuant to the SISP, and information was not forthcoming from BSI and the Proposal Trustee on what their intention was leading up to the comeback hearing date of October 5, 2018. Those concerns were again set out in a letter from BDC to BSI dated October 1, 2018. This letter was not acknowledged by BSI.

***The Third Extension to the Stay of Proceedings***

12. On October 5, 2018 BDC once again appeared before this Honourable Court, at which time BSI sought a third extension to the stay of proceedings under section 50.4(9) of the BIA. BDC and its counsel did not receive BSI's materials for the October 5, 2018 hearing until late in the afternoon on October 4, 2018 and did not receive the report of the Proposal Trustee until after close of business on October 4, 2018.

13. BSI provided BDC with two documents to support its October 5, 2018 application to seek yet another stay of proceedings. The first was a draft terms letter from a company called "Next Edge Capital" (the "**NextEdge Letter**"), appearing to be a lender based in Ontario, and the second being a non-binding letter of intent from Heddle Marine Inc. (the "**Heddle Offer**").

14. In the report filed by the Proposal Trustee, officer of this Honourable Court, the Proposal Trustee took no position on whether or not the further extension should be granted. This was in stark contrast to the position taken by the Proposal Trustee in BSI's previous extension applications where the Proposal Trustee supported the extension in order to continue with the SISP and attempt to present a viable proposal. BSI nonetheless sought the additional extension without the support and recommendation of the Proposal Trustee.

15. BDC took the position that the NextEdge Letter contained uncertain and unworkable terms and the non-binding Heddle Offer, being the only expression of interest, was so low that it could never be accepted by BSI. As such, BDC submitted that it did not support either the NextEdge Letter or the Heddle Offer and that neither of these options warranted a further extension to the stay of proceedings. Notwithstanding BDC's submissions and the lack of support from the Proposal Trustee, this Honourable Court granted a further extension to the stay of proceedings until October 26, 2018.

16. Since the October 5, 2018 hearing, BDC has not received a draft proposal or evidence of a binding offer from BSI. BDC has not received any update on the cash flow of the company. BDC has received email communication indicating that BSI had provided Heddle Marine with a counter-offer, to which BSI gave Heddle Marine until October 17,

2018 to respond. The October 17, 2018 deadline has now passed, and on October 19, 2018, BDC was advised that the original Heddle Offer, which BDC believes to be unacceptable, would not be revised. Furthermore, BDC has not received any letters of offer from NextEdge, or any other potential refinancing lenders BDC can only conclude that there is neither an offer to purchase nor a refinancing offer to be received by BSI in the immediate future.

17. BDC's concerns continue to grow, as notwithstanding the considerable passage of time and numerous extensions to the stay of proceedings, BSI has not demonstrated that it is capable of making a viable proposal. These concerns were again set out in a letter from BDC to BSI dated October 15, 2018, which letter was not acknowledged by BSI.

## PART II – ISSUES

18. BDC submits that the following issues need to be determined and are addressed in this memorandum of fact, law and argument:

    a. Is BSI entitled to have a fourth extension to the stay of proceedings granted pursuant to section 50.4(9) of the BIA?

## PART II – LAW & ARGUMENT

19. BDC states that, pursuant to section 50.4(9) of the BIA, the stay of proceedings can only be extended if BSI has acted in good faith and with due diligence, is likely to be able to make a viable proposal if the extension is granted, and if no creditor will be materially prejudiced if the extension is granted.

20. Section 50.4(9) of the BIA states:

> The insolvent person may, before the expiry of the 30-day period referred to in subsection (8) or of any extension granted under this subsection, apply to the court for an extension, or further extension, as the case may be, of that period, and the court, on notice to any interested persons that the court may direct, may grant the extensions, not exceeding 45 days for any individual extension and not exceeding in the aggregate five months after the expiry of the 30-day period referred to in subsection (8), if satisfied on each application that
>
> (a) the insolvent person has acted, and is acting, in good faith and with due diligence;

(b) the insolvent person would likely be able to make a viable proposal if the extension being applied for were granted; and

(c) no creditor would be materially prejudiced if the extension being applied for were granted.

***Bankruptcy and Insolvency Act*, RSC 1985, c B-3, s 50.4(9) [TAB 1]**

21. The law is clear that in order for BSI to be granted an extension, it has the onus of demonstrating that it satisfies each of the three elements of the test. As stated in *Plancher Heritage Ltee/Heritage Flooring Ltd., Re* (2004), "*the debtor must prove on the balance of probabilities that an extension is justified*".

***Plancher Heritage Ltee/Heritage Flooring Ltd., Re* [2004] N.B.J. No 286 [TAB 2]**

22. The fact that BSI satisfied the test in its previous applications is not determinative. BSI continues to bear the burden of proof on each subsequent application. This point was clarified as follows in the case of *Entegrity Wind Systems Inc., Re,* 2009 PESC 33:

> [5] Entegrity met all three branches of the test in its initial application for an extension of time, but each of those three branches must be now revisited to determine whether Entegrity continues to meet its legal requirements for a further extension as its efforts since August 19, 2009 may demonstrate.

***Entegrity Wind Systems Inc., Re,* 2009 PESC 33 [TAB 3]**

23. If BSI cannot satisfy each element of the test, this Honourable Court must exercise its discretion to dismiss this application for a fourth extension to the stay of proceedings. BDC states that it is appropriate, in this case, for this Honourable Court to exercise this discretion.

***Has BSI acted in good faith and with due diligence?***

24. While BDC did not dispute BSI's submission that it was acting in good faith and with due diligence during its previous applications, it is becoming increasingly evident that BSI is no longer acting in good faith and with due diligence in order to complete the preparation of a viable proposal.

25. Similar to the case in *Entegrity Wind Systems Inc.*, where the Court concluded that the debtor failed on this prong of the test, BSI has simply floated the non-binding

discussions between Next Edge and Heddle Marine as potential options, asserting in previous applications that it required more time to bring these options to fruition. No additional information has been provided to BDC with respect to the development of these options and it is clear that they will not represent the basis of a viable proposal. Further, BSI has indicated on more than one occasion, most notably during the September 21, 2018 comeback hearing, that it would not continue to pursue further extensions of the stay if there were no legitimate and workable expressions of interest. Notwithstanding this representation, BSI has continued to seek the extension of time, further eroding BDC's position.

26. Similar facts were present in *Entegrity Wind Systems Inc.*, which lead the PEI Supreme Court to conclude that the debtor was no longer acting in good faith and with due diligence. The Court's analysis and conclusion with respect to these facts and this element of the test are summarized at paragraphs 18 and 19 of the decision as follows:

> [18] In my view, Entegrity has attempted to recast its argument on good faith and due diligence that carried it through the day in its original application...it floated the name of Valmont Industries as one target which it felt would invest in the company but more time was needed to bring that to fruition...
>
> [19] It is now October, 2009, and we have nothing more from Valmont, not even an indication in writing that they are interested in Entegrity. Add to that the reference to Pure Energy and to Western Community Energy, and in my view all you have is pure fluff. There is no substance here. Entegrity has failed to meet the first part of the test. In my view it was not acted in good faith and with due diligence.

27. BDC submits that this Honourable Court should apply the PEI Supreme Court's analysis and conclude that BSI has failed on this element of the section 50.4(9) test.

***Would BSI likely be able to make a viable proposal if the extension were granted?***

28. In the case of *Baldwin Valley Investors Inc., Re* [1994] O.J. No. 271, two related debtor companies filed a notice of intention to file proposals under the BIA, and each subsequently received an extension to file a proposal. When the companies failed to file a proposal by the extended time, they applied for an additional stay which was denied by the Registrar in Bankruptcy and subsequently by the Ontario Court of Justice on

Appeal. In this case, Justice Farley summarized the manner in which to apply this element of the test as follows:

> [4] It seems to me that "viable proposal" should have to take on some meaning akin to one that seems reasonable on its face to the "reasonable creditor"...it does not appear to me that the debtor companies have shown that they are likely to be able to make a viable proposal. While that need not be a certainty: see my views at pp. 10-11 in *Re Cumberland Trading Inc.* released January 24, 1994..."Likely" as defined in *The Concise Oxford Dictionary of Current English*, 7th ed. (1987; Oxford, The Claredone Press) means:
>
> > *likely* 1. Such as *might well happen*, or turn out to be the thing specified; *probable* 2. to be *reasonably expected.* [emphasis added]
>
> I do not see the conjecture of the debtor companies' rough submission as being *"likely"*.

***Baldwin Valley Investors Inc., Re* [1994] O.J. No. 271 [TAB 4]**

29. It is evident based on this interpretation that it is not "likely" that BSI will be able to submit a viable proposal. There have not been any developed or legitimate expressions of interest put forward that could lead to the conclusion that a viable proposal is likely. Furthermore, unlike in the case of *Baldwin Valley Investors Inc.*, there is not even a draft proposal for this Honourable Court to consider, nor does BSI's cash-flow statement demonstrate that it is on its way to developing a viable proposal. With the ceasing of operations leading to insignificant cash receipts, the cash flow is being consistently eroded by professional fees, as demonstrated in the Proposal Trustee's last report. This erosion, coupled with the lack of sale or refinancing alternatives, demonstrate starkly that a viable proposal has not been proved.

30. The facts here are also not unlike the case in *Royalton Banquet & Convention Centre Ltd., Re,* 2007 Carswell Ont. 3796, where the Ontario Superior Court of Justice also dismissed the debtor's application for an extension of time to file a proposal. The Court's analysis and conclusion with respect to these facts and this element of the test are summarized at paragraphs 18 and 19 of the decision as follows:

> [18] On its own material the applicant is deficient in this regard. In paragraph 11 of the affidavit of the president of the applicant he swears that the:

> [applicant] requires an extension of time to file its Proposal in order to continue efforts to resolve outstanding disputes and to determine the most advantageous terms for a restructuring and any possible related transactions. If [the applicant] is granted the extension, I am hopeful that [the applicant] will be able to make a viable proposal to its creditors within the extension period being sought.
>
> [19]As I said at the hearing and as counsel agreed, being "hopeful" of winning the lottery is not the same as it being "likely". To quote Mr. Justice Farley in *Benson v Third Canadian General Investment Trust Ltd.* [1993 CarswellOnt 166 (Ont. Gen. Div. [Commercial List]) "If wishes were horses, then beggars will ride." There is no evidence before me that a proposal is likely. Counsel for the applicant conceded that based on the status of the relationship between the applicant and the respondent, the only type of proposal that is even conceivable at this time is a liquidation proposal. That is not what is implied by the applicant's affidavit, and as a result I find that the granting of the extension will not likely result in a viable proposal.

***Royalton Banquet & Convention Centre Ltd., Re*, 2007 Carswell Ont. 3796 [TAB 5]**

31. Similarly, in the case at bar, the prospect of a viable proposal is simply wishful thinking at this point in time. It is evident based on the evidence that a viable proposal is not likely and a further extension of the stay of proceedings cannot be granted on the basis of a mere possibility. The fact that the Proposal Trustee has not supported BSI's request for an extension speaks further to the fact that a viable proposal is not likely.

32. BDC therefore submits that BSI has not shown that it is likely to be able to make a viable proposal and, as such, this Honourable Court should find that BSI has failed on this element of the section 50.4(9) test.

***Will any creditor be materially prejudiced if the extension being applied for were granted?***

33. In *Bennett on Bankruptcy*, a leading authority on bankruptcy and insolvency in this country, the editors address the issue of the material prejudice element of the section 50.4(9) test:

> The insolvent person has the onus of proof in applying for an extension and, at that time, the insolvent person must demonstrate that the creditors will not be "materially prejudiced". This may be a difficult take for a debtor where the security of the secured creditor is diminishing, depreciating, or declining in value. For example, if the value of the security drops below the debt, the secured creditor can argue that its position is prejudiced...In considering the degree of prejudice, the

court reviews and number of factors in deciding whether creditors are materially prejudiced.

While the debtor may obtain an initial 10-day stay of proceedings from secured creditors, and perhaps longer, a secured creditor who holds substantially most of the debt will likely be successful in terminating the proposal process or in lifting the stay of proceedings to appoint a receiver if it wishes to exercise its rights.

**Frank Bennett, *Bennett on Bankruptcy*, 14th Edition 2012, at pp. 190-191 [TAB 6]**

34. BDC is the secured creditor holding substantially most of the debt and therefore bears the greatest economic risk. Being the main economic interest holder, BDC is and will continue to be further materially prejudiced by another extension of the stay of proceedings. While BDC has been unable to enforce its security, it has been forced to stand by while its prospects of full recovery continue to deteriorate without any recourse or opportunity to intervene. This material prejudice may be mitigated if BSI is deemed bankrupt and a trustee takes control of the assets of BSI and attempts to put BSI in a viable position.

35. BDC submits that it relies on the following factors to demonstrate that it will be materially prejudiced if another extension is granted:

a. BSI has been in default of its obligations since July 11, 2018, and the total secured indebtedness to BDC as at October 18, 2018 is $1,177,712.04;

b. each day that passes erodes BDC's security, and the total indebtedness continues to rise. It is becoming less and less likely that the SISP process will provide for any meaningful recovery by BDC;

c. the passage of time renders the possibility of salvaging BSI's operations more and more remote;

d. BDC has lost confidence in the ability of BSI to put forth a viable proposal;

e. BSI is not seeking to be sold as a going concern enterprise and as such, this proceeding is not about a restructuring of an ongoing business, but rather a veiled liquidation. An assignment in bankruptcy is more appropriate for a liquidation of BSI and less prejudicial for its creditors.

f. If BSI is deemed to have made an assignment in bankruptcy, all of the assets of BSI will vest in its Trustee in Bankruptcy, thereby preserving those assets, and the Trustee has the power to operate the company, under the oversight of this Honourable Court;

g. BSI has offered no evidence on this application for a fourth extension of time as to how it will mitigate or avoid the material prejudice to BDC. The issue of material prejudice to BDC has not been addressed in any substantive way by BSI, notwithstanding the onus being on BSI to establish a lack of material prejudice.

36. It is evident based on the foregoing factors that it is more likely than not the BDC will suffer material prejudice if the requested extension is granted.

37. Similarly, in *Entegrity Wind Systems Inc.*, the court held that the debtor failed on this element of the test, concluding that it was more likely than not that the secured creditor would suffer material prejudice if the extension was granted. In reaching this conclusion, the Court considered many factors put forth by the creditor to demonstrate material prejudice, many of which were similar to those concerns of BDC outlined above. The Courts conclusion was summarized as follows:

> [35] The question I must ask myself is whether it is more likely than not that Mercantile [the creditor] will suffer material prejudice if the requested extension is granted? After considering the arguments advanced by both parties, I am of the view that Mercantile would suffer material prejudice and therefore Entegrity [the debtor] has failed to satisfy the third branch of the test. This material prejudice exhibits itself not simply in the amount which is currently owed by Entegrity to Mercantile and the per diem that continues to pile up since Entegrity's default, but it is the accumulation of all those other factors referred to by Mercantile which would further erode its position if the extension were granted.

38. BDC therefore submits that BSI has not shown that no creditors will be materially prejudiced by the extension of the stay and, as such, this Honourable Court should find that BSI has failed on this element of the section 50.4(9) test.

## PART III – RELIEF SOUGHT

39. Based on all of the foregoing reasons, BDC submits that it is clear that BSI will be unable to discharge the onus on it as set out in s. 50.4(9) of the BIA. Accordingly, BDC respectfully asks this Honourable Court for the following:

1. To exercise its discretion to dismiss BSI's application for a further extension to the stay of proceedings; and
2. to grant a corresponding Order stating that BSI is now deemed to have made an assignment in bankruptcy pursuant to section 50.4(8) of the BIA.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED**

**DATED** at St. John's, Newfoundland and Labrador this 23 day of October, 2018

for **Darren D. O'Keefe**
**Solicitor for BDC**
Cox & Palmer
Suite 1100, Scotia Centre
235 Water Street
St. John's, NL A1C 1B6

**APPENDIX A**

***List of Authorities***

TAB 1

**Bankruptcy and Insolvency Act (R.S.C. (Revised Statutes of Canada), 1985, c. B-3)**
Act current to 2018-10-03 and last amended on 2018-05-23.

**PART III**

# Proposals (continued)

**DIVISION I**

## General Scheme for Proposals (continued)

**Secured creditor may file proof of secured claim**

**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.

**Proposed assessed value**

**(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.

**Idem**

**(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.

**Idem**

**(4)** Where a secured creditor is dissatisfied with the proposed assessed value of his security, the secured creditor may apply to the court, within fifteen days after the proposal is sent to the creditors, to have the proposed assessed value revised, and the court may revise the proposed assessed value, in which case the revised value henceforth applies for the purposes of this Part.

**Where no secured creditor in a class takes action**

**(5)** Where no secured creditor having a secured claim of a particular class files a proof of secured claim at or before the meeting of creditors, the secured creditors having claims of that class shall be deemed to have voted for the refusal of the proposal.

1992, c. 27, s. 19; 1997, c. 12, s. 31(F).

**Excluded secured creditor**

**50.2** A secured creditor to whom a proposal has not been made in respect of a particular secured claim may not file a proof of secured claim in respect of that claim.

1992, c. 27, s. 19.

**Rights in bankruptcy**

**50.3** On the bankruptcy of an insolvent person who made a proposal to one or more secured creditors in respect of secured claims, any proof of secured claim filed pursuant to section 50.1 ceases to be valid or effective, and sections 112 and 127 to 134 apply in respect of a proof of claim filed by any secured creditor in the bankruptcy.

1992, c. 27, s. 19.

**Notice of intention**

**50.4 (1)** Before filing a copy of a proposal with a licensed trustee, an insolvent person may file a notice of intention, in the prescribed form, with the official receiver in the insolvent person's locality, stating

**(a)** the insolvent person's intention to make a proposal,

**(b)** the name and address of the licensed trustee who has consented, in writing, to act as the trustee under the proposal, and

**(c)** the names of the creditors with claims amounting to two hundred and fifty dollars or more and the amounts of their claims as known or shown by the debtor's books,

and attaching thereto a copy of the consent referred to in paragraph (b).

**Certain things to be filed**

**(2)** Within ten days after filing a notice of intention under subsection (1), the insolvent person shall file with the official receiver

**(a)** a statement (in this section referred to as a "cash-flow statement") indicating the projected cash-flow of the insolvent person on at least a monthly basis, prepared by the insolvent person, reviewed for its reasonableness by the trustee under the notice of intention and signed by the trustee and the insolvent person;

**(b)** a report on the reasonableness of the cash-flow statement, in the prescribed form, prepared and signed by the trustee; and

**(c)** a report containing prescribed representations by the insolvent person regarding the preparation of the cash-flow statement, in the prescribed form, prepared and signed by the insolvent person.

**Creditors may obtain statement**

**(3)** Subject to subsection (4), any creditor may obtain a copy of the cash-flow statement on request made to the trustee.

**Exception**

**(4)** The court may order that a cash-flow statement or any part thereof not be released to some or all of the creditors pursuant to subsection (3) where it is satisfied that

**(a)** such release would unduly prejudice the insolvent person; and

**(b)** non-release would not unduly prejudice the creditor or creditors in question.

**Trustee protected**

**(5)** If the trustee acts in good faith and takes reasonable care in reviewing the cash-flow statement, the trustee is not liable for loss or damage to any person resulting from that person's reliance on the cash-flow statement.

**Trustee to notify creditors**

**(6)** Within five days after the filing of a notice of intention under subsection (1), the trustee named in the notice shall send to every known creditor, in the prescribed manner, a copy of the notice including all of the information referred to in paragraphs (1)(a) to (c).

**Trustee to monitor and report**

**(7)** Subject to any direction of the court under paragraph 47.1(2)(a), the trustee under a notice of intention in respect of an insolvent person

**(a)** shall, for the purpose of monitoring the insolvent person's business and financial affairs, have access to and examine the insolvent person's property, including his premises, books, records and other financial documents, to the extent necessary to adequately assess the insolvent person's business and financial affairs, from the filing of the notice of intention until a proposal is filed or the insolvent person becomes bankrupt;

**(b)** shall file a report on the state of the insolvent person's business and financial affairs — containing the prescribed information, if any —

**(i)** with the official receiver without delay after ascertaining a material adverse change in the insolvent person's projected cash-flow or financial circumstances, and

**(ii)** with the court at or before the hearing by the court of any application under subsection (9) and at any other time that the court may order; and

**(c)** shall send a report about the material adverse change to the creditors without delay after ascertaining the change.

**Where assignment deemed to have been made**

**(8)** Where an insolvent person fails to comply with subsection (2), or where the trustee fails to file a proposal with the official receiver under subsection 62(1) within a period of thirty days after the day the notice of intention was filed under subsection (1), or within any extension of that period granted under subsection (9),

**(a)** the insolvent person is, on the expiration of that period or that extension, as the case may be, deemed to have thereupon made an assignment;

**(b)** the trustee shall, without delay, file with the official receiver, in the prescribed form, a report of the deemed assignment;

**(b.1)** the official receiver shall issue a certificate of assignment, in the prescribed form, which has the same effect for the purposes of this Act as an assignment filed under section 49; and

**(c)** the trustee shall, within five days after the day the certificate mentioned in paragraph (b.1) is issued, send notice of the meeting of creditors under section 102, at which meeting the creditors may by ordinary resolution, notwithstanding section 14, affirm the appointment of the trustee or appoint another licensed trustee in lieu of that trustee.

**Extension of time for filing proposal**

**(9)** The insolvent person may, before the expiry of the 30-day period referred to in subsection (8) or of any extension granted under this subsection, apply to the court for an extension, or further extension, as the case may be, of that period, and the court, on notice to any interested persons that the court may direct, may grant the extensions, not exceeding 45 days for any individual extension and not exceeding in the aggregate five months after the expiry of the 30-day period referred to in subsection (8), if satisfied on each application that

**(a)** the insolvent person has acted, and is acting, in good faith and with due diligence;

**(b)** the insolvent person would likely be able to make a viable proposal if the extension being applied for were granted; and

**(c)** no creditor would be materially prejudiced if the extension being applied for were granted.

**Court may not extend time**

**(10)** Subsection 187(11) does not apply in respect of time limitations imposed by subsection (9).

**Court may terminate period for making proposal**

**(11)** The court may, on application by the trustee, the interim receiver, if any, appointed under section 47.1, or a creditor, declare terminated, before its actual expiration, the thirty day period mentioned in subsection (8) or any extension thereof granted under subsection (9) if the court is satisfied that

**(a)** the insolvent person has not acted, or is not acting, in good faith and with due diligence,

**(b)** the insolvent person will not likely be able to make a viable proposal before the expiration of the period in question,

**(c)** the insolvent person will not likely be able to make a proposal, before the expiration of the period in question, that will be accepted by the creditors, or

**(d)** the creditors as a whole would be materially prejudiced were the application under this subsection rejected,

and where the court declares the period in question terminated, paragraphs (8)(a) to (c) thereupon apply as if that period had expired.

1992, c. 27, s. 19; 1997, c. 12, s. 32; 2004, c. 25, s. 33(F); 2005, c. 47, s. 35; 2007, c. 36, s. 17; 2017, c. 26, s. 6(E).

**Date modified:**

2018-10-18

TAB 2

2004 NBBR 168, 2004 NBQB 168
New Brunswick Court of Queen's Bench

Plancher Heritage Ltée / Heritage Flooring Ltd., Re

2004 CarswellNB 358, 2004 NBBR 168, 2004 NBQB 168, [2004]
N.B.J. No. 286, 279 N.B.R. (2d) 1, 3 C.B.R. (5th) 60, 732 A.P.R. 1

# In the Matter of The Proposal of Plancher Heritage Ltée / Heritage Flooring Ltd.

Glennie J.

Judgment: July 20, 2004
Docket: 10543, Estate No. 51-114608

Counsel: G. Patrick Gorman, Q.C. for Heritage Flooring Ltd.
Stephen J. Hutchinson, Jeffrey R. Parker, Lee C. Bell-Smith for Royal Bank of Canada

Subject: Insolvency; Civil Practice and Procedure
**Related Abridgment Classifications**
Bankruptcy and insolvency
VI Proposal
VI.1 General principles
**Table of Authorities**
**Cases considered by *Glennie J.*:**

*Baldwin Valley Investors Inc., Re* (1994), 23 C.B.R. (3d) 219, 1994 CarswellOnt 253 (Ont. Gen. Div. [Commercial List]) — considered

*Bell ExpressVu Ltd. Partnership v. Rex* (2002), 2002 SCC 42, 2002 CarswellBC 851, 2002 CarswellBC 852, 100 B.C.L.R. (3d) 1, [2002] 5 W.W.R. 1, 212 D.L.R. (4th) 1, 287 N.R. 248, 18 C.P.R. (4th) 289, 166 B.C.A.C. 1, 271 W.A.C. 1, 93 C.R.R. (2d) 189, [2002] 2 S.C.R. 559 (S.C.C.) — referred to

*Com/Mit Hitech Services Inc., Re* (1997), 1997 CarswellOnt 2753, 47 C.B.R. (3d) 182 (Ont. Bktcy.) — considered

*Cumberland Trading Inc., Re* (1994), 23 C.B.R. (3d) 225, 1994 CarswellOnt 255 (Ont. Gen. Div. [Commercial List]) — considered

*Gene Moses Construction Ltd., Re* (1999), 1999 CarswellBC 149, 9 C.B.R. (4th) 275 (B.C. Master) — considered

*National Bank of Canada v. Dutch Industries Ltd.* (1996), 149 Sask. R. 317, 45 C.B.R. (3d) 103, 1996 CarswellSask 631 (Sask. Q.B.) — referred to

*Scotia Rainbow Inc. v. Bank of Montreal* (2000), 2000 CarswellNS 216, 18 C.B.R. (4th) 114, (sub nom. *Scotia Rainbow Inc. (Bankrupt) v. Bank of Montreal)* 186 N.S.R. (2d) 153, (sub nom. *Scotia Rainbow Inc. (Bankrupt) v. Bank of Montreal)* 581 A.P.R. 153 (N.S. S.C.) — referred to

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

s. 50(1.5) [en. 1992, c. 27, s. 18(1)] — considered

s. 50.4(1) [en. 1992, c. 27, s. 19] — referred to

s. 50.4(8) [en. 1992, c. 27, s. 19] — referred to

s. 50.4(11) [en. 1992, c. 27, s. 19] — referred to

s. 50.4(11)(b) [en. 1992, c. 27, s. 19] — referred to

s. 50.4(11)(c) [en. 1992, c. 27, s. 19] — referred to

s. 65.1(1) [en. 1992, c. 27, s. 30] — considered

s. 65.1(4) [en. 1992, c. 27, s. 30] — considered

s. 65.1(4)(b) [en. 1992, c. 27, s. 30] — considered

s. 69 — referred to

ss. 69-69.3(1) — referred to

ss. 69-69.31 — referred to

s. 69(1) — referred to

s. 69(1)(a) — referred to

s. 69.4 [en. 1992, c. 27, s. 36(1)] — considered

s. 244 — referred to

MOTION by insolvent company for extension of stay under s.69 of *Bankruptcy and Insolvency Act* and for order that bank return to it all funds taken from its operating accounts.

***Glennie J.*:**

1 On February 11, 2004, Plancher Heritage Ltee / Heritage Flooring Ltd. ("Heritage") filed a Notice of Intention To Make A Proposal (the "Notice of Intention") pursuant to Subsection 50.4(1) of the *Bankruptcy and Insolvency Act* (the "BIA"). A.C. Poirier & Associates Inc. (the "Trustee") consented to act as Trustee under the proposal. Section 69 of the BIA grants a stay (the "Stay") of all creditor actions and remedies against the insolvent person, which stay in this case was to expire on March 12, 2004. On March 12, 2004, I extended the Stay in this matter to Thursday, March 25, 2004 and advised that I would file written reasons for the granting of such an extension. These are those reasons.

2 There is also another issue, namely whether Heritage's banker, Royal Bank of Canada (the "Bank") operated contrary to the stay by sweeping Heritage's operating account and capping its available line of credit or whether the Bank is authorized to do so by virtue of Section 65.1(4)(b) of the BIA.

**Background**

3 Heritage manufactured hardwood flooring at its plant in Kedgwick, New Brunswick. It had annual gross sales in the range of five to six million dollars.

4 On January 30, 2001, Heritage accepted an offer from the Bank's Asset Based Finance Division to establish a revolving credit facility in favour of Heritage with a credit limit of two million dollars subject to the limitation that the aggregate amount of borrowings under the credit facility was at no time to exceed the facility borrowing base which was defined in the offer from the Bank to Heritage as follows:

> "Facility Borrowing Base" means at the date of determination, an amount equal to the aggregate of all Eligible Accounts Receivable multiplied by 85% with an exception for those accounts which are insured by Export Development Corporation, which will be multiplied by 90% until April 30, 2001 at which time the advance rate for Eligible Accounts Receivable will reduce to 85%; and Eligible Inventory, multiplied by 60% capped at $1,500,000.00

reducing to $1,000,000.00 at April 30, 2001, less any stated Reserve, as determined by the Bank from time to time in its sole discretion.

5 The Bank's credit facility was structured as an asset based loan under which the Bank amends its available credit weekly based upon reported details from Heritage on the status of its accounts receivable and inventory.

6 Pursuant to the January 30, 2001 loan agreement (the "Loan Agreement"), the Bank agreed to make financing available to Heritage on the basis of the value of its assets and the security of its accounts receivable and inventory under the Bank's Asset - Based Finance Model (the "ABF model").

7 According to the Bank, the ABF Model is a unique financial product which enables its customers to immediately access increased levels of financing on the basis of the fluctuating value of their inventory and their accounts receivable. According to the Bank, the ABF model is based on aggressive margining, with very few required financial covenants, to highly leveraged businesses. The operative components of the ABF model are as follows:

(a) receipts from the sale of inventory are deposited to a blocked account for immediate application against the balance outstanding under the customer's operating facility;

(b) an uploaded reporting of inventory/accounts receivable valuation information is provided by the customer to the Bank on a weekly basis;

(c) the inventory/accounts receivable valuation reporting establishes the level of funding available under the operating facility for the upcoming week and

(d) the ongoing monitoring and built in control mechanism imposed through the use of the blocked account enables the Bank to provide immediate advances against the value of the customer's inventory and accounts receivable in amounts substantively higher than would be available under traditional lending models (i.e. eighty-five percent (85%) of eligible accounts receivable and up to a maximum of sixty percent (60%) of inventory values, subject to ongoing appraisals, margined on a weekly basis, compared with the standard margining levels available under the Bank's traditional lending models, which is (75%) of accounts receivable and (50%) of inventory, margined on a monthly basis).

8 In order to monitor and manage its collateral base, it is typical for the Bank to implement this type of cash management arrangement through the blocked account in order to match advances to the value of the underlying assets. Receipts are deposited in the blocked account in order to replace collateral sold in support of previous advances made, until the next opportunity to value the collateral base which is the basis for extensions of credit. At no time is the borrower under the ABF model deprived of the use of its cash since it receives credit for those receipts deposited to the blocked account which are then re-advanced on the basis of the margining formula to which the parties have agreed. Advances are typically made on a weekly basis but can be made on a more frequent basis provided that a calculation of the borrowing base (based upon eligible accounts receivable and inventory) can be made. The Bank charged Heritage a monthly "*monitoring fee*" of $4,500.00.

9 Heritage also entered into a Blocked Accounts Agreement with the Bank as of March 8, 2001. The Blocked Accounts Agreement provided that all cash, including all cheques, money orders, wire transfers and other remittances payable to Heritage on account of its accounts receivable, debts and book debts of any nature, are to be deposited to the blocked account.

10 In order to access funds using the ABF Model, Heritage was required to submit the required weekly upload to the Bank in order to determine current levels of accounts receivable and inventory of Heritage. The Bank's system then calculated the total amount of available credit based upon the inventory accounts receivable valuation and compared this with the outstanding amount previously advanced under the credit facility. The difference (assuming the total amount of available credit is higher than the amount previously advanced) made up the available credit to Heritage. This amount

would then be deposited to Heritage's operating account through which Heritage would access the funds for working capital purposes.

11 On the business day following the deposit of receipts by Heritage to the blocked account, the funds are applied against the outstanding amount under the credit facility in order to replace the collateral used to generate these receipts. For example, if the facility was drawn to $800,000.00 and Heritage deposited $300,000.00 to the blocked account, this amount would be applied against the loan thus reducing the balance to $500,000.00. Heritage would then submit an upload; the Bank would calculate availability based on the current level of eligible inventory and accounts receivable, and assuming the total availability is determined to be $700,000.00, compared to the outstanding debt of $500,000.00, then availability to Heritage would be $200,000.00. This $200,000.00 would then be deposited by the Bank to the operating account for access by Heritage in the ordinary course.

12 The credit facility established by the Loan Agreement was for an initial term of two years ending on January 30, 2003 and was to be automatically renewed for successive 180 day periods unless either Heritage or the Bank gave prior written notice of termination to the other, not less than 90 days in advance of the end of the initial term or successive term.

13 According to the Trustee, Heritage maintained its covenants and margin position with the Bank with the exception of one instance in January of this year when it became out of margin as a result of two large customer receivables extending beyond the authorized 90 day aging period. According to the Trustee, this situation was remedied immediately by Heritage authorizing the Bank to return two cheques that had been presented for payment. However, in a letter to Heritage dated February 2, 2004 from Counsel for the Bank, Heritage was advised that it was in default of the provisions of the margin working Capital Loan Agreement between Heritage and the Bank dated February 14, 2001 "*particularly in connection with its financial covenants thereunder and the financial condition of the Corporation.*" The letter went on to state "*The Bank also has concerns regarding the Corporation's continued financial performance and its current financial ratios.*"

14 The Bank did not provide details of the alleged default by Heritage nor did it allow Heritage time to remedy such default, but instead advised Heritage that it no longer wished to continue its business relationship with it and then demanded payment of all indebtedness of Heritage to the Bank to be paid in full within 15 days from the date of the February 2, 2004 demand letter.

15 In October of 2003, Heritage requested that the Bank renew the Credit facility for a further year. According to the Trustee, Heritage requested a response from the Bank regarding its extension request at least every two weeks since the request was made. In January of 2004, with no response having been received from the Bank, Heritage began requesting a 90-day extension of the credit facility to April 30, 2004. Heritage says that no response was ever received from the Bank regarding the renewal request. Heritage says that no written response was received from the Bank until it received the letter from the Bank's solicitors on February 2, 2004 containing a demand for payment in full of all of the indebtedness of Heritage to the Bank within 15 days. The demand letter was accompanied by a Notice of Intention to enforce security pursuant to Section 244 of the BIA. It was also dated February 2, 2004.

16 In response to the Bank's demand for payment, Heritage filed its Notice of Intention to make a Proposal pursuant to Subsection 50.4(1) of the BIA on February 11, 2004.

17 It should be noted that in early November of 2003, Claude Alexander, a Senior Manager, Portfolio Risk, of the Bank contacted Gilbert LeBlanc, the President of Direcsys Inc. to ascertain if he might be available to assist Heritage in a restructuring of its business. Mr. Alexander also inquired if funding might be available from the Atlantic Canada Opportunities Agency ("ACOA") and the Province of New Brunswick to pay Mr. LeBlanc's fees. Mr. Alexander's call to Mr. LeBlanc subsequently led to financing being approved for Mr. LeBlanc's fees. As well, an Adjustment Committee, which Mr. LeBlanc described as a mini board of directors was established for Heritage on December 27, 2003. This committee was comprised of various representatives of stakeholders including ACOA, the Province of New Brunswick, the Restigouche Economic Development Corporation and Heritage and Mr. LeBlanc.

18 On February 12, 2004, the Trustee wrote to Counsel for the Bank advising that Heritage had filed a Notice of Intention to Make a Proposal and also that the Trustee expected that the Bank would honour the requirement to allow Heritage to continue to use its operating account at the Bank on a cash basis, in other words, that the Bank would freeze the amount of the account at the close of business on February 11, 2004 and that further activity in the account would be done on a cash basis with Heritage having full access to deposits made on or after February 12, 2004.

19 On February 16, 2004, Counsel for the Bank wrote to the Trustee as follows:

*As you and I have discussed and as I mentioned in my recent voicemail message to you, the Bank wishes Heritage all the best in its endeavours to restructure its business and is willing to cooperate as much as possible with a view to Heritage reaching these goals. In this regard, the Bank has agreed that during the stay period, Heritage may continue to use its operating account with the Bank on a cash-basis, but that the Bank will not provide overdraft privileges. The Bank also acknowledges the maintenance of the status quo during the period of the stay, and is happy to allow Heritage the time to consider and develop its Proposal.*

*As you may know, the Bank has security over all property, real and personal, of Heritage and margins the company's inventory and accounts receivable pursuant to the credit facility made available to Heritage by the Bank, by way of a Margin Working Capital Loan Agreement dated January 30, 2001 (the "Agreement"). This arrangement contemplates the deposit of all monies received by Heritage in payment of its accounts receivable to a blocked account, which ensures that the Bank's security position is maintained on a steady basis, such that credit made available based upon eligible inventory, for example, is directly secured by the account(s) generated by the sale of that inventory. This is the only way in which such an asset-backed loan may remain secured, and the only way, in the current situation, that the Bank's security position will not be materially prejudiced during the stay period. The Bank therefore requires that this procedure be continued, and that all remaining financial and other reporting by Heritage pursuant to the Agreement continue, including, without limitation, a detailed weekly perpetual inventory listing, as contemplated thereby. The Bank has capped the amount of available credit pursuant to the facility as of the date of the filing of the Notice, and as such, when deposits are made to the blocked account, utilization of the facility will be reduced accordingly. The balance, constituting the difference between the capped facility amount and the amounts so deposited to the blocked account, shall be made available to Heritage, upon the same margins and subject to the same conditions of the existing arrangement pursuant to the Agreement.*

*As you know, the* Bankruptcy and Insolvency Act *(Canada) provides that a creditor shall not be materially prejudiced by the operation of the stay pursuant to the Proposal provisions thereof, and that the security position of a secured creditor shall remain materially unaffected thereby. Therefore, while the Bank is willing to cooperate as much as possible with Heritage and the trustee in connection with the ongoing situation, it will obviously not allow its secured position to be prejudiced by the dissipation of secured assets, without replacement thereof so as to maintain the status quo.*

20 On February 20, 2004, the Trustee wrote to Counsel for the Bank as follows:

You advised us that the Royal Bank had taken funds from the Debtor's account. This morning, the Debtor advised us that your client has seized over $200,000 from the Debtor's account, without any authorization. The Royal Bank has, in our view, enforced its security in contravention of the stay of proceedings that is in place by virtue of section 69 of the Bankruptcy and Insolvency Act.

We are also dismayed by the Royal Bank's actions as we were in discussions with you regarding alternative ways to satisfy the Royal Bank that it's position was not being materially prejudiced. In addition, we wrote to you on February 13, 2004 advising that we were advising the Debtor that it was safe to deposit funds into their account as the Bank would honor the cash based operation of the account. A copy of that letter is attached. In our view, the Royal Bank's has acted in bad faith towards the Trustee in the Proposal and towards the Debtor who is legitimately attempting to restructure its affairs in accordance with the provisions of the Bankruptcy and Insolvency Act.

Based on the actions of the Royal Bank, we have advised the Debtor that they should make no more deposits to the Royal Bank.

We request that the funds seized by the Royal Bank be returned immediately to the Debtor's account. The failure to return the funds may cause irreparable harm to the Debtor's efforts to restructure its affairs and may cause damage to the Debtor and to other stakeholders affected by the Royal Bank's actions.

21 On February 23rd, Counsel for the Bank responded to the Trustee advising that, in his opinion, the Bank had not exercised secured remedies and that the Bank was acting in accordance with the contractual arrangements in place between the Bank and Heritage where under the Bank agreed to make financing available to Heritage under the security of its accounts receivable and inventory under the Bank's ABF model. The letter went on to state:

*The Notice of Intention To Make A Proposal under the BIA was filed by Heritage on February 11, 2004. On that date the upload which had been provided to the Bank by Heritage on February 10, 2004 confirmed Heritage was entitled to the $1,283,444.74 outstanding under the operating facility. In accordance with Section 65.1(4)(b) of the BIA, the Bank capped the operating facility at this amount and has agreed, subject to Heritage's compliance with the terms of the asset backed model, to provide Heritage with ongoing access to the operating facility up to this amount.*

[Emphasis added.]

*Funds in the appropriate amount of $200,000.00 were deposited with the Bank by Heritage subsequent to February 11, 2004 and were applied by the Bank against the operating facility in the usual course. The Bank did not make a demand, exercise any remedy or take any action to enforce its security, it simply continued to act in accordance with the established contractual arrangement. Heritage submitted a further upload of financial information to the Bank on February 20, 2004. This upload revealed a decrease in the Bank's security position of approximately $140,000.00 in the nine days subsequent to the filing of the Notice of Intention. Based upon this upload and the $200,000.00 deposited by Heritage with the Bank during the same period, Heritage has current availability under its operating facility in the amount of $61,317.00. These funds would not have been made available to Heritage in the normal course until two days following receipt of the upload. The Bank facilitated the immediate availability of these funds to Heritage on February 20, 2004 as a consequence of your advice that Heritage required an immediate advance of funds. The Bank also processed a debit memo earlier on February 20, 2004, in respect Heritage's payroll, with a view to avoiding any disruption in Heritage's business operations.*

*Notwithstanding the foregoing, you have now demanded that Heritage be provided with immediate access to the $200,000.00 deposited by Heritage with the Bank subsequent to the filing of the Notice of Intention. You appear to be proceeding on the basis the "asset backed model" is not of application following the filing of the Notice of Intention. We note that if the Bank were to acquiesce to this request, the effect would be that the Bank's security position would have deteriorated by approximately $140,000.00 in nine days since the filing of the Notice of Intention. We do not regard this position as tenable or reasonable and believe it is expressly contrary to the status quo intent of the BIA. We note the Bank is not seeking to improve its position, and remains willing to make funding available to Heritage on the basis of the "asset lending model" on the go forward. Compliance with your request would prejudice the Bank's position and in effect constitute a further advance of credit, which the Bank is not required to provide pursuant to subsection 65.1(4)(b) of the BIA. The bottom line is Heritage cannot pursue its restructuring through a systematic erosion of the Bank's security position.*

*As previously discussed, the Bank is willing to co-operate with Heritage in its goal of restructuring its business pursuant to the proposal provisions of the BIA. However, the Bank cannot be materially prejudiced in the process and Heritage cannot expect to finance its restructuring by eroding the value of the Bank security. We understand that you have advised Heritage to make no further deposits with the Bank.*

*The Bank requires that Heritage confirm that all cash receipts on a go-forward basis shall continue to be deposited to the blocked account, that uploads continue to be made on a weekly basis and Heritage continue to comply with the terms of its asset lending model arrangement with the Bank.*

22 On February 25, 2004, Heritage filed a motion seeking an extension of the stay and also an order that the Bank return to it all funds taken from its operating accounts since February 11, 2004 and that the Stay be extended to April 12, 2004.

23 The Bank opposed Heritage's motion and subsequently filed its own motion seeking an order declaring the 30-day period for filing a proposal terminated pursuant to Sections 50.4(11)(b) and (c) of the BIA or, in the alternative a declaration that Sections 69 to 69.3(1) of the BIA no longer operate in respect of the Bank pursuant to Section 69.4 of the BIA and, in the further alternative, an order determining the classes of secured creditors pursuant to Subsection 50(1.5) of the BIA and in so doing determine that the Bank does not fall within the same class of secured creditors as Business Development Bank of Canada and Farm Credit Corporation.

24 Counsel for the Bank argued that Heritage would not likely be able to make a viable proposal before the expiration of the 30-day period that will be accepted by the creditors of Heritage and that the Bank is likely to be materially prejudiced by the continued operations of Sections 69 - 69.31 of the BIA.

25 The Bank argued that its level of security decreased significantly after the filing by Heritage of the Notice of Intention. The Bank says that in the nine days following the filing, its level of security decreased in the approximate amount of $140,000.00. Five days later, on February 25, 2004, the Bank says its position had been eroded by a further amount of approximately $38,000.00.

26 Immediately prior to the filing of the Notice of Intention, Heritage was entitled to draw upon its credit facility at the Bank in the amount of $1,283,444.74. Subsequently, Heritage made significant deposits to its Canadian dollar operating account and its U.S. dollar operating account. On the date of filing of the Notice of Intention, the Bank capped Heritage's credit facility at the then current outstanding balance of $1,283,444.74.

27 Subsequent to the filing of its Notice of Intention, Heritage made deposits to its Canadian account and its U.S. account totalling $209,944.03. Subsequent to the deposits being made by Heritage, the Bank transferred the deposited funds to the blocked account and swept the funds in what the Bank says was in accordance "*with the existing contractual arrangements with Heritage.*" The balance outstanding under the credit facilities was thus reduced to $1,080,589.38. The Trustee advised counsel for the Bank that the Bank's action offended the Stay in place as a result of the filing of the Notice of Intention. He went on to state, "*the actions of the bank could have a damaging affect on the debtor's ability to restructure.*" The Trustee notified counsel for the Bank that Heritage had confirmed to him that the Bank had seized $205,445.01 from Heritage's account and the Trustee requested the immediate return of the funds.

28 The Bank argued that if it had not reduced the amount of the loan balance through the sweep of the account in the usual process. The Bank says it would, as of March 1, 2004, have been in a margin deficit of $179,984.88 in the 14 days since the filing of the Notice of Intention due to a decrease of the level of the Bank's security from $1,283,529.43, as of the date of filing of the Notice, to $1,103,544.55 as of the February 25, 2004 upload. The Bank argued that a decrease of approximately $180,000.00 in the level of its security over a period of 14 days amounted to material prejudice and that the stay should not be allowed to continued.

29 The Trustee takes the position that the Bank's action in sweeping the account was in contravention of the Stay and that the Bank should be ordered to replace the funds and be restrained from taking any further action in this regard without further order of this Court. The Trustee also asserts that the Bank has not been materially prejudiced.

**The Application For An Extension Of Time**

30 Subsection 50.4(9) of the BIA provides:

> 69.(1) Subject to subsections (2) and (3) and sections 69.4 and 69.5, on the filing of a notice of intention under section 50.4 by an insolvent person,
>
> > (a) no creditor has any remedy against the insolvent person or the insolvent person's property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy.

31 I am satisfied, on a balance of probabilities, that as of March 12, 2004 Heritage met the following criteria to grant an extension: a) It had acted, and continued to act, in good faith and with due diligence; b) It would likely be able to make a viable proposal if the extension were to be granted; and, c) no creditor of Heritage would be materially prejudiced if the extension were to be granted.

32 The test for whether Heritage would likely be able to make a viable proposal, if granted the extension, is whether it would likely, as opposed to certainly, be able to present a viable proposal. The test is not whether or not a specific creditor would be prepared to support the proposal. In *Baldwin Valley Investors Inc.* (1994), 23 C.B.R. (3d) 219 (Ont. Gen. Div. [Commercial List]), Justice Farley was of the opinion that "viable" means "reasonable on its face" to a reasonable creditor and that "likely" did not require certainty but meant "might well happen", "probable" or "to be reasonably expected." See also *Scotia Rainbow Inc. v. Bank of Montreal* (2000), 18 C.B.R. (4th) 114 (N.S. S.C.).

33 In support of its motion, the Bank relied on Section 50.4(11)(c) of the BIA and argued that Heritage would not be able to make a proposal before the expiration of the 30-day period that would be accepted by the majority of its creditors. It relied upon *Cumberland Trading Inc., Re*, [1994] O.J. No. 132 (Ont. Gen. Div. [Commercial List]) in support of its argument. In *Cumberland Trading Inc.*, Skyview International Finance Corporation represented 95 percent of the value of the claims of secured creditors of Cumberland and 67 percent of all creditors' claims. Skyview therefore had a veto power on any vote on a proposal and it asserted that there was no proposal which Cumberland could make that it would approve. Justice Farley allowed Skyview's motion and declared terminated the 30-day period in which to file a proposal.

34 Similarly, in *Com/Mit Hitech Services Inc., Re*, [1997] O.J. No. 3360 (Ont. Bktcy.), Toronto Dominion Bank ("TD Bank") was owed more than 90 percent of the debtor's total indebtedness and brought a motion pursuant to Section 50.4(11) of the BIA requesting a declaration that the 30-day period provided in Section 50.4(8) be terminated. Justice Farley allowed TD Bank's application, recognizing that TD Bank was the overwhelming creditor and thus was in a veto position with respect to any proposal.

35 However, in the present case, the Trustee has advised that the Bank would be outside the terms of any proposal and would in fact be paid out. As well, Gilbert LeBlanc testified that Group Savoie, which has expressed an interest in acquiring all of the outstanding shares of Heritage, understands that the Bank would have to be paid out. Accordingly, the Bank's argument that it is in a position to veto any proposal put forth by Heritage must fail since the Trustee has advised that the Bank will not be in a position to veto any proposal since it will be outside the terms of any proposal and would not be included in any class of creditors of Heritage.

36 In granting an extension of the stay, I relied on the fact that Groupe Savoie Inc. expressed a desire to negotiate with the shareholders of Heritage for the purpose of structuring a transaction whereby it would acquire all of the outstanding shares of Heritage. It was anticipated that negotiations would take place from March 15th to March 17, 2004 "*with a formal letter of intent to be provided no later than Monday, March 22, 2004 and open for acceptance by the shareholders of the Company until 5:00 p.m. on Tuesday, March 23, 2004.*" Groupe Savoie is an arms length corporation with substantial assets.

37 At the time of the hearing of Heritage's motion, I was satisfied that Heritage established on a balance of probabilities that an extension was justified. Accordingly, I allowed Heritage's application for an extension of the Stay to March 25, 2004.

**The Availability of Credit**

38 The next issue to be addressed is whether the Bank acted contrary to the Stay provisions of Section 69 of the BIA by sweeping Heritage's operating account and capping its operating facility subsequent to the date Heritage filed its Notice Of Intention. Heritage argues that by so doing the Bank in effect executed a remedy contrary to Section 69.(1) of the BIA.

39 Section 69 of the BIA provides:

> 69.(1) Subject to subsections (2) and (3) and sections 69.4 and 69.5, on the filing of a notice of intention under section 50.4 by an insolvent person,
>
> > (a) no creditor has any remedy against the insolvent person or the insolvent person's property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy.

40 In *Gene Moses Construction Ltd.* (1999), 9 C.B.R. (4th) 275 (B.C. Master) the Court held that a secured creditor could not remove money from the debtor's account after the filing of a Notice of Intention. The debtor's motion for an order that the funds be returned was granted. The Court held that "*remedy*" in Section 69 must be given a broad interpretation.

41 In *National Bank of Canada v. Dutch Industries Ltd.* (1996), 45 C.B.R. (3d) 103 (Sask. Q.B.), National Bank unsuccessfully applied to the Court to lift the Stay imposed by the filing of a Notice of Intention to Make a Proposal. National Bank had continued to demand the debtor meet its margin requirements and continued to take the funds from the debtor's bank account. The Court stated at ¶ 10:

> ... The applicant argued that s. 69(1)(b) of the Act did not prevent it from insisting upon, not did it release the debtor from the obligation of complying with the margining requirements arising under the credit agreements existing between the parties. Section 69(1)(b) provides that no provision in a security agreement which provides that in these circumstances the insolvent ceases to have rights to use and deal with assets secured under the agreement "as he would otherwise have" has any force and effect. It appears the margin requirements imposed by the Bank under the existing arrangements would result in its seizing or having the right to seize the cash receipts of the business. In such circumstances the respondents would be unable to continue its business. As such a situation would effectively negate the stay of proceedings, it cannot be allowed to prevail. However, the respondents must be prevented from allowing the material erosion of the security of the Bank and s. 69(4) gives the Court power to make provisions for protection of the creditor, suspending the stay fully or upon a qualified basis if the creditor is likely to be materially prejudiced by the stay.

42 As was the situation in the case of Heritage, Dutch Industries opened an account at another bank and started making its deposits to that account. The Court allowed that arrangement to continue, provided an accounting was made daily to National Bank and subject to other terms and conditions imposed by the Court.

43 The stay of proceedings provisions contained in Section 69 of the BIA are designed to prevent proceedings by a creditor which might give that creditor an advantage over other creditors. See: *The 2004 Annotated Bankruptcy and Insolvency Act* by Lloyd W. Houlden and Jeffery B. Morawetz, at F § 53.

44 Counsel for the Bank argued that in accordance with Section 65.1(4)(b) of the BIA, the Bank had kept the operating facility at the amount outstanding on February 10, 2004, the date prior to the date of Heritage's filing of its Notice of Intention. In other words, it capped the credit facility at that moment in time. As a consequence of the capping of

available credit, utilization by Heritage of its credit facility would be reduced accordingly when it made deposits to its blocked account. The Trustee demanded that Heritage be provided with immediate access to the funds deposited by Heritage with the Bank subsequent to the filing of the Notice of Intention. Counsel for the Bank argued that the Bank was not seeking to improve its position and remains willing to make funds available to Heritage on the basis of the "*Asset Lending Model on the go forward.*" He went on to state, "*compliance with your request would prejudice the Bank's position and in effect constitute a further advance of credit which the Bank is not required to provide pursuant to Subsection 65.1(4)(b) of the BIA.*"

45 Section 65.1(4) of the BIA provides as follows:

> (4) Certain acts not prevented - nothing in subsections (1) to (3) shall be construed
>
> (a) as prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided after the filing of
>
> (i) the notice of intention, if one was filed, or
>
> (ii) the proposal, if no notice of intention was filed; or
>
> (b) as requiring the further advance of money or credit.

46 There is an obvious contradiction in the position taken by the Bank with respect to the continued use by Heritage of its operating account with the Bank. On the one hand the Bank "*acknowledges the maintenance of the status quo during the period of the stay.*" On the other, the Bank capped the amount of available credit pursuant to the credit facility as of the date of filing of the Notice of Intention and would only provide Heritage with ongoing access to its operating facility up to that amount. The Bank has stated that under the ABF model, at no time would the borrower be deprived of the use of its cash since it receives credit for those receipts deposited to its blocked account "*which are then re-advanced on the basis of the margining formula to which the parties have agreed.*"

47 The Bank asserts that it has the authority to cap the operating facility by virtue of Section 65.1(4)(b) of the BIA. It argues that compliance with the request of Heritage would "*in effect constitute a further advance of credit, which the Bank is not required to provide pursuant to Subsection 65.1(4)(b).*" I disagree with the Bank's interpretation in this regard.

48 I interpret the provisions of Section 65.1(4)(b) of the BIA to mean that the status quo is intended by the BIA to be protected and preserved. Neither party to a loan agreement can unilaterally amend its terms. Failure to maintain the status quo would be contrary to the fundamental objective of the stay provisions of the BIA as they relate to an insolvent person being authorized to file a Proposal.

49 In interpreting the scope of the BIA's rights and remedies, the modern approach to statutory interpretation should be applied. The words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament: *Bell ExpressVu Ltd. Partnership v. Rex*, [2002] 2 S.C.R. 559 (S.C.C.), at para 26, citing E.A. Driedger, *Construction of Statutes* (2nd ed. 1983), at p. 87.

50 In my view, the purpose of the relevant stay provisions legislated by the BIA is to preserve and protect the status quo at the moment in time an insolvent person files a Notice Of Intention To Make A Proposal. In this particular case, I am of the view that Heritage was entitled to avail itself of the revolving credit facility it accepted from the Bank on January 30, 2001 subject to the terms and conditions contained therein. That facility should continue to be operated in accordance with its terms and conditions notwithstanding the filing by Heritage of a Notice Of Intention. The capping by the Bank of the amount available to Heritage would in effect constitute a unilateral change or amendment to those terms and conditions.

51 In the February 23rd letter from Counsel for the Bank to the Trustee, it is stated that the Bank "*remains willing to make funding available to Heritage on the basis of the 'asset lending model' on the go forward.*" The stay of proceedings protection established by the BIA maintains the status quo. In my opinion, by capping the revolving line of credit, the Bank in effect exercised a remedy against Heritage contrary to the BIA's stay provisions. The intention of the stay provisions contained in the BIA is to allow an insolvent person to continue its business in accordance with its existing arrangements with its creditors, which in the case of a bank or other secured creditor would be in accordance with its existing authorized credit agreements. In my view, a secured creditor cannot unilaterally amend a loan or credit agreement relating to a secured revolving line of credit by capping the available line of credit particularly during the reasonable period of time to repay timeline. Obviously, there is a dispute between the Bank and Heritage with respect to whether Heritage was in default of any of its covenants to the Bank at the time of the issuance of the Bank's Demand for payment. There is also the issue of the inventory discrepancy which came to light during the hearing. As a consequence of that discrepancy, it is not possible to determine the issue of whether the Bank should return the money it swept from Heritage's account. It is only possible to comment generally on the availability of credit in a case such as this which involves a revolving line of credit.

52 In *ComMit Hitech Services Inc., Re, supra*, TD Bank sought a declaration under Section 50.4(11) of the BIA that the 30 day period be terminated, or, alternatively, an order that Section 69 of the BIA no longer operated in respect of TD Bank. As mentioned, TD Bank's motion was allowed. The debtor cross-applied for an order restraining TD Bank from interfering with the banking relationship. The cross-motion was dismissed.

53 Justice Farley writes at ¶ 11:

> *The Bank's extension of credit was on a demand basis. The Debtor is in material breach of the terms of that demand loan. There would not appear to me in the circumstances to be any requirement of continuing the line of credit intact including allowing the Debtor to call upon the unused portion thereof given the breach and additionally because of the demand. Section 244(2) of the BIA is aimed at providing enforcement of security not at the provision of new money. Section 65.1(4)(b) provides that s. 65.1(1), (2) and (3) do not require "the further advance of money* or *credit" (emphasis added). In respect of the demand, it should be noted that I am not commenting upon whether the line of credit should continue to exist during the "reasonable period of time to repay" period. However, in that regard I would note that the Bank continued to honour cheques for 6 days after its demand. But as well to my mind it is important to appreciate that there were material breaches of a number of important covenants and that it was a demand as opposed to term loan. I do not see that there is any validity to the Debtors claim for relief; I would dismiss its cross motion.*

54 It is relevant to note that in *ComMit Hitech Services Inc.*, Justice Farley found that the debtor in that case was not acting in good faith and with due diligence. There were material breaches of a number of important covenants. The character of the debtor as a borrower from TD Bank had changed significantly from when the banking relationship commenced and more importantly from when the then existing loan arrangements were made. TD Bank demanded payment and issued a Section 244 Notice pursuant to the BIA on July 10, 1997. On December 12, 1996, TD Bank advised the debtor that it was in breach of its credit conditions. On January 15, 1997, TD Bank offered an amended arrangement which was accepted by the debtor. The debtor was to fulfill certain conditions, but only carried out one of those conditions. In fact, Justice Farley concluded that the debtor was "*going essentially in a 180° way against what was agreed to in January, 1997.*"

55 In the present case, the letter dated February 2, 2004 from the Bank's lawyers refers to Heritage's Credit Facility as a "*Revolving Demand Operating Facility*" [Emphasis added.] The offer of the facility from the Bank dated January 30, 2001 offered Heritage "*a revolving credit facility*" with the word '*demand*' noticeably absent. The Default provisions provide that in the event of a default under any agreement in respect of the borrowed money or if there was "*in the Bank's opinion*", a material adverse change in the "*financial condition, or operation or ownership*" of Heritage, all indebtedness of Heritage to the Bank would, at the option of the Bank, become immediately due and payable.

56 The February 2, 2004 demand for payment states that Heritage was in default of the "*Margin Working Capital Loan Agreement*" between Heritage and the Bank and that the Bank also had concerns regarding Heritage's "*continued financial performance and its current financial ratios.*" It does not specify what the default was nor does it afford Heritage time to cure the default. The demand letter went on to state that the Bank no longer wished to continue its business relationship with Heritage and required payment in full of all indebtedness of Heritage to the Bank within 15 days.

57 The purpose of the BIA's stay provisions as incorporated in Section 69 is to maintain the status quo. In my opinion, maintaining the status quo does not include the capping of a debtor's secured revolving line of credit during which would otherwise be available to the debtor had it not filed a Notice Of Intention to Make a Proposal. The receipts deposited by Heritage to its blocked account should have continued to be re-advanced to Heritage by the Bank on the basis of the margining formula to which the parties had agreed. The Bank has stated that under the ABF model a Borrower would "*at no time*" be deprived by the use of its cash, since cash receipts are re-advanced based upon the margining formula. The Bank is protected because it has set the margin requirements for Heritage's revolving line of credit. Its security, the receivables and inventory, continue to revolve and if there is a reduction of either, the amount of credit available would accordingly be reduced based upon the margining formula established by the Bank. Counsel for the Bank stated in a letter to the Trustee, "*The bottom line is Heritage cannot pursue its restructuring through a systematic erosion of the Bank's security position.*" In my opinion, as long as the margin requirements are being met, there would be no erosion of the Bank's security on Heritage's inventory and receivables.

58 In *Com/Mit Hitech Services Inc.*, Justice Farley was of the view that the debtor was not acting in good faith and with due diligence. On the issue of whether the debtor could avail itself of a continuing line of credit, he concluded that in the circumstances of that case, there did not appear to be any requirement of continuing the line of credit intact including allowing the debtor to call upon the unused portion thereof given the material breaches of a number of covenants and that it was a demand as opposed to a term loan.

59 In the present case, the Credit Facility offered by the Bank to Heritage and accepted by it on January 30, 2001 was for an initial term of two years ending on January 30, 2003 and then automatically renewed itself for successive 180 day periods unless either Heritage or the Bank gave prior written notice to the other not less than 90 days in advance of the end of the initial term or successive term.

60 As mentioned, the Bank's February 2, 2004 demand letter cited that Heritage was in default of the Margin Capital Loan Agreement but does not specify what the default was nor does it afford Heritage an opportunity to cure or remedy the default. It also stated the Bank had concerns regarding Heritage's "*continued financial performance and its current financial ratios.*" These ratios were not specified, nor was the default.

61 It must also be remembered that it was the Bank that took the initiative to put Mr. LeBlanc in place to try to find a buyer for Heritage. The Bank's initiative also resulted in the appointment of an advisory committee which was in place at the time the Bank issued its demand for payment.

62 I mention this because it goes to the issue of what a reasonable period to meet the demand for payment might have been in this case. At the time the demand for payment was issued by the Bank, there were no payments overdue since it was a revolving line of credit. The Trustee says Heritage was not in default of its loan conditions.

63 Although the Bank asserted in the letter from its Counsel dated February 2, 2004 that Heritage was in default of the Margin Capital Loan Agreement, Heritage claimed that it maintained its covenants and margin position with the exception of one instance in January 2004 which it claims was remedied "*immediately.*" The Trustee stated that Heritage's Credit Facility with the Bank did not have an expiration date until January 31, 2004.

64 I acknowledge there is an inventory discrepancy problem in this case which was not discerned until after the various motions in this matter were filed. As a consequence of this discrepancy, it is not possible to determine on the limited evidence before me if the Bank ought to return the funds it swept from Heritage's account after February 11, 2004.

65 The most that can be said is that both a debtor and a secured creditor have defined rights under the BIA which must be applied to the facts of each individual fact situation.

66 On the one hand, there is a secured creditor's right to call a loan and demand payment and to issue a Notice of Intention to Enforce Security pursuant to Section 244 of the BIA, provided it is entitled to do so in accordance with the loan agreements in place between it and its debtor. On the other, there is the debtor's right to file a Notice of Intention to Make a Proposal pursuant to Section 50.4(1) of the BIA.

67 In my opinion, the issue of the type of loan, namely demand, term, or revolving, is relevant in the context of whether a secured creditor is required to continue to operate existing credit agreements in accordance with loan agreements in place with the debtor.

68 In Houlden and Morawetz, *Bankruptcy and Insolvency Analysis* The authors, the Hon. L.W. Houlden and Geoffrey B. Morantz, write:

> *If the security which the secured creditor wishes to enforce is a demand loan, it would seem that the security holder should make a demand for payment before giving the notice under s. 244(1), because it could be argued that until the demand period has expired, the creditor cannot have "and intention to enforce his security". If the security agreement calls for term payments and a payment is overdue, then there seems no reason why the notice under s. 244(1) could not be combined with a Lister v. Dunlop notice: Prudential Assurance Co. (Trustee of) v. 90 Eglinton Ltd. Partnership* supra; *Delron Computers Inc. v. Peat Marwick Thorne Inc., [1995] 5 W.W.R. 174, 31 C.B.R. (3d) 75, 1985 CarswellSask 5 (Sask.Q.B.).*

69 In an article entitled '*Enforcement of Security - The Battle of the Notices*' by Andrew B. Laidlaw, 37 C.B.R. (3d), the author writes at page 282:

> *The loan may be expressed to be repayable in full on a specified date, or by instalments, each due on a specified date. In such cases, there is no place for the common law doctrine of reasonable time to pay, because the borrower knows in advance when his or her payment obligations become due.*
>
> *A different situation arises when a loan agreement provides that the whole of the outstanding loan will immediately become due and payable without the need for demand upon the occurrence of a specified default, for instance, the failure to pay an instalment of principal or interest, the breach of a financial covenant, or failure to pay a sum due under another agreement. In* Kavcar, *McKinlay J.A. said, at p. 17:*
>
> > I am satisfied that so long as the debtor is not misled, the creditor may rely on any default by the debtor when making a demand for payment whether or not the specific default is outlined in the letter of demand. However, I do not accept Aetna's argument that some types of default permit enforcement of the security without any demand for payment being made. In my view, the law has developed to the point where, regardless of the wording of a debenture security, it cannot be enforced without, first, the making of a demand, and second, the giving of a reasonable time within which to pay the indebtedness. This was the opinion of Fawcus J. in *Royal Bank v. Cal Glass Ltd.* [(1979), 18 B.C.L.R. 55], at p. 68, and I agree.
>
> *This judicial statement should not be read as meaning that a loan cannot immediately become due and payable without demand, or as meaning that security cannot become enforceable without demand: McKinlay J.A. is simply saying that a secured creditor cannot actually enforce its security without making demand and then giving the debtor a reasonable time to pay.*

70 In the case of Heritage, the Bank demanded payment of its indebtedness within 15 days from February 2, 2004. Whether or not 15 days is a reasonable time period in the circumstances of this case is not to be determined on this motion. I mention this issue in this context because, in my opinion, the Bank should have continued operating Heritage's

revolving line of credit in accordance with agreements in effect at the time of the Bank's demand. In other words, I am of the view that the Bank had no authority to cap Heritage's line of credit as of the day immediately proceeding the filing by Heritage of its Notice of Intention to Make a Proposal. The revolving line of credit should have continued to be operated in accordance with the terms and conditions agreed to between the Bank and Heritage. The Bank established the receivable and inventory margins at the outset when it offered the revolving line of credit to Heritage.

71 The BIA establishes the Stay of Proceedings provision in Section 69(1). Clearly, a secured creditor can not enforce its security during the stay period. The intention of the legislation is to maintain the status quo while the debtor attempts to reorganize.

72 Section 65.1(1) of the BIA provides that where a notice of intention or a proposal has been filed in respect of an insolvent person, no person may terminate or amend any agreement with the insolvent person, or claim an accelerated payment under any agreement with the insolvent person.

73 The section goes on to provide that this is not to be construed as "*requiring the further advance of money or credit.*" However, in the case of a revolving line of credit, such as in this case, in my view the Bank would be re-advancing Heritage's receipts which it had deposited to its blocked account. In other words, it is not advancing additional credit, rather it is simply a revolving process operating in accordance with the margins and conditions agreed to by both Heritage and the Bank. In the February 23rd letter from Counsel for the Bank to the Trustee, it is stated that the Bank "*remains willing to make funding available to Heritage on the basis of the 'asset lending model' on the go forward.*" As mentioned, the Bank has stated that under the ABF model, a borrower would at no time be deprived of the use of its cash since it receives credit for those receipts deposited to its blocked account "*which are then re-advanced on the basis of the margining formula to which the parties have agreed.*" [Emphasis added.] That is the essence of a revolving line of credit. Section 65.1(4) of the BIA must be read in context of the Bank's agreements with Heritage. The Bank is required to "*re-advance*" the cash receipts received by Heritage in accordance with the margining formula.

74 On the one hand, the Bank is not permitted to amend its loan agreements with Heritage by, for example, capping the available line of credit, however, it is not required to make a further advance of money or credit. As can be seen, this issue is somewhat complicated in the case of a revolving line of credit. Based upon the agreed formula for inventory and receivable margins, the Bank is in effect allowing Heritage to use the funds it has collected from its customers and deposited to its blocked account with the Bank. The Bank has represented that "*at no time is the borrower under the ABF model deprived of the use of its cash since it receives credit for those receipts deposited to the blocked account which are then re-advanced on the basis of the margining formula to which the parties have agreed.*" [Emphasis added.] In my view, this process is simply the use by Heritage of the funds it has collected from its customers and deposited to its blocked account. As the Bank has stated, it is the borrower's "*cash.*" In other words, the Bank is not making a fresh advance of its money or giving new credit over and above that which was agreed to and in full force and effect at the time of filing by Heritage of its Notice of Intention to Make a Proposal. It is simply giving Heritage credit the receipts it deposited to the blocked account.

75 In any event, if a secured creditor is in doubt as to its obligations due to the interplay between the Stay of Proceedings provision contained in Section 69(1) of the BIA and the notwithstanding provisions contained in section 65.1(1), it can apply for an order declaring the thirty day period for a debtor to file a proposal terminated pursuant to Section 50.4(11) of the BIA or a declaration that Sections 69 to 69.31 of the BIA no longer operate in respect of that creditor pursuant to Section 69.4 of the BIA.

76 Section 69.4 provides:

> A creditor who is affected by the operation of sections 69 to 69.3 may apply to the court for a declaration that those sections no longer operate in respect of that creditor, and the court may make such a declaration, subject to any qualifications that the court considers proper, if it is satisfied

(a) that the creditor is likely to be materially prejudiced by the continued operation of those sections; or

(b) that it is equitable on other grounds to make such a declaration.

77 This is the procedure the Bank followed in this case, namely a motion seeking a termination under Section 50.4(11) and a declaration pursuant to Section 69.4 of the BIA.

78 In *Cumberland Trading Inc.*, *supra*, Justice Farley comments on the meaning of the words "*materially prejudiced*" as contained in Section 69.4 of the BIA. He writes at paragraph 11:

> ¶ Is Skyview entitled to the benefit of s. 69.4(a) BIA? I am of the view that the material prejudice referred to therein is an objective prejudice as opposed to a subjective one - i.e., it refers to the degree of the prejudice suffered vis-à-vis the indebtedness and the attendant security and not to the extent that such prejudice may affect the creditor qua person, organization or entity. If it were otherwise then a "big creditor" may be so financially strong that it could never have the benefit of this clause. In this situation Skyview's prejudice appears to be that the only continuing financing available to Cumberland is that generated by turning Cumberland's accounts receivable and inventory (pledged to Skyview) into cash to pay operating expenses during the period leading up to a vote on a potential proposal, which process will erode the security of Skyview, without any replenishment. However Skyview does not go the additional step and make any quantitative (or possibly qualitative) analysis as to the extent of such prejudice so that the court has an idea of the magnitude of materiality. In other words, Skyview presently estimates that it would be fortunate to realize $450,000 on Cumberland's accounts receivables and inventory, but it does not go on to give any foundation for a conclusion that in the course of the next month $x of this security would be eaten up or alternatively that the erosion would likely be in the neighbourhood of $y per day of future operations. The comparison would be between the "foundation" of a maximum of $450,000 and what would happen as to deterioration therefrom if the stay is not lifted. I note there was no suggestion by Cumberland that there would be no erosion of Skyview's position by, say, getting cash injection or by improving margins by increasing revenues or decreasing expenses. Skyview's request for its first relief request is dismissed since in my view Skyview did not engage in the correct comparison of material prejudice.

79 In *Com/Mit Hitech Services Inc.*, *supra*, Justice Farley writes at ¶ 7:

> ¶ 7 I considered the question of material prejudice as to s. 50.4(11) and s. 69.4 in Re Cumberland Trading Inc. (1994), 23 C.B.R. (3d) 225 (Ont. Gen. Div.). In this present case, there was no evidence as to value either on a going concern, liquidation or other basis. Based upon the worst cash flow information given by the Debtor, the erosion of assets would be approximately $50,000 per month. Thus before the Bank would have the opportunity of opposing an extension of time to make the proposal would only be another three weeks (with a possible erosion on that basis of some $35,000 - $40,000). Given the relative magnitudes, I do not see that the Bank has made out the aspect of material prejudice. There was no specific argument as to s. 69.4(b) regarding "it is equitable on other grounds to make such a declaration." Thus it would not appear to me that the Bank should succeed on the basis of s. 50.4(11)(d) or its alternate request for relief under s. 69.4.

**Conclusion**

80 At the time of the hearing of Heritage's motion for an extension of the stay, it had established that such an extension was justified, and was so granted.

81 With respect to the availability of credit, I am of the view that Heritage would be entitled, notwithstanding its filing of a Notice Of Intention under the BIA on February 11, 2004, to avail itself of the revolving credit facility established by the Loan Agreement in accordance with its terms under the ABF model, and in particular in accordance with the margin requirements established by the Bank.

82 In my opinion, the Bank was not entitled to sweep Heritage's operating account and cap the amount available to Heritage as of the date of its filing of a Notice Of Intention to Make a Proposal. Heritage was entitled to the use of its cash receipts which it had deposited to the blocked account in accordance with its agreement with the Bank. By unilaterally capping Heritage's revolving credit facility, the Bank exercised a remedy contrary to the stay provisions of the BIA. To conclude otherwise would negate the purpose of the stay provisions of the BIA and the fundamental objective of maintaining the status quo while an insolvent person attempts to reorganize.

83 The terms and conditions of the revolving credit facility in place between the Bank and Heritage should have remained in full force and effect notwithstanding the filing by Heritage of a Notice Of Intention To Make A Proposal

*Motion granted.*

**End of Document**

TAB 3

2009 PESC 33
Prince Edward Island Supreme Court

Entegrity Wind Systems Inc., Re

2009 CarswellPEI 63, 2009 PESC 33, 181 A.C.W.S. (3d) 424, 291 Nfld. & P.E.I.R. 175, 898 A.P.R. 175

# In the Matter of the Notice of Intention to make a Proposal of Entegrity Wind Systems Inc. (Insolvent Person) and Pricewaterhousecoopers Inc. (Trustee)

In the matter of a Motion by Entegrity Wind Systems Inc. having a place of business in Charlottetown, Prince Edward Island, to grant a further extension for filing a Proposal pursuant to Section 50.4 of the Bankruptcy and Insolvency Act

Wayne D. Cheverie J.

Heard: October 9, 2009
Judgment: October 15, 2009
Docket: S1 BK-2429

Counsel: Pamela J. Williams for Applicant, EWSI
Kevin Kiley, Michael Drake for Respondent, Mercantile Finance Services Ltd.

Subject: Insolvency

**Related Abridgment Classifications**

Bankruptcy and insolvency
VI Proposal
VI.2 Time period to file
VI.2.a Extension of time

**Table of Authorities**

**Cases considered by *Wayne D. Cheverie J.*:**

*Baldwin Valley Investors Inc., Re* (1994), 1994 CarswellOnt 253, 23 C.B.R. (3d) 219 (Ont. Gen. Div. [Commercial List]) — considered

*Cantrail Coach Lines Ltd., Re* (2005), 10 C.B.R. (5th) 164, 2005 BCSC 351, 2005 CarswellBC 581 (B.C. Master) — considered

*Entegrity Wind Systems Inc., Re* (2009), 56 C.B.R. (5th) 1, 2009 PESC 25, 2009 CarswellPEI 47 (P.E.I. S.C.) — referred to

*Mercantile Finance Services Ltd. v. Entegrity Wind Systems Inc.* (2009), 2009 PESC 23, 288 Nfld. & P.E.I.R. 352, 888 A.P.R. 352, 2009 CarswellPEI 46 (P.E.I. S.C.) — referred to

*Nortec Colour Graphics Inc., Re* (2000), 18 C.B.R. (4th) 84, 2000 CarswellOnt 2797 (Ont. Bktcy.) — considered

**Statutes considered:**

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

s. 50.4 [en. 1992, c. 27, s. 19] — referred to

s. 50.4(1) [en. 1992, c. 27, s. 19] — referred to

s. 50.4(9) [en. 1992, c. 27, s. 19] — considered

***Wayne D. Cheverie J.*:**

**Introduction**

1 Entegrity Wind Systems Inc. ("Entegrity") brings this motion for an order pursuant to s-s. 50.4 (9) of the *Bankruptcy and Insolvency Act* R.S.C. 1985 Cap. B-3 as amended R.S.C. 1985 Cap. 27 first supplement ("the Act") for a further extension of 45 days in which to file a proposal to its creditors. Entegrity filed its Notice of Intention to Make a Proposal pursuant to s-s. 50.4(1) of the Act on July 15, 2009. It failed to produce its proposal within the initial 30 days allowed by the Act, and applied for and was granted an initial extension of 45 days by court order dated August 19, 2009. I presided over that hearing and granted that court order, with reasons (see In *Entegrity Wind Systems Inc., Re*, 2009 PESC 25 (P.E.I. S.C.)).

2 Entegrity is insolvent. As such, it invoked the provisions of s. 50.4 of the Act and engaged Pricewaterhousecoopers Inc. as its trustee and then filed its Notice of Intention to Make a Proposal. With its initial 30-day period coming to an end, and it not having developed its proposal, Entegrity applied for an extension of 45 days. It successfully argued before me that it was acting in good faith and with due diligence; would likely be able to make a viable proposal if the extension were granted; and that no creditor would be materially prejudiced if the extension were granted. A key consideration in granting that extension was my acceptance of the factual underpinning as argued by Entegrity. In short, Entegrity made a case for an extension based on its inability to focus on obtaining additional funding sources because it was preoccupied with the actions taken by its primary creditor, Mercantile Finance Services Ltd. ("Mercantile").

3 Entegrity still bears the burden of proof to satisfy the court on the balance of probabilities that it has complied with the law and is thus entitled to ask for a further extension of time in which to file its proposal. As in the previous application, Entegrity's motion is opposed by Mercantile. What must be determined is whether Entegrity has discharged its burden by satisfying the three-part test articulated by Parliament in s-s. 50.4(9) of the Act. Put more directly, what has Entegrity done since my order of August 19, 2009 to demonstrate that it is deserving of a further 45-day extension?

**The Law**

4 In a sense, Parliament has codified the rules governing an extension of time for filing a proposal. Extensions are discretionary and may only be granted if the court is satisfied that the requirements of s-s. 50.4(9) of the Act are met. That subsection states:

> (9) Extension of time for filing proposal - The insolvent person may, before the expiration of the thirty day period mentioned in subsection (8) or any extension thereof granted under this subsection, apply to the court for an extension, or further extension, as the case may be, of that period, and the court may grant such extensions, not exceeding forty-five days for any individual extension and not exceeding in the aggregate five months after the expiration of the thirty day period mentioned in subsection (8), if satisfied on each application that
>
> (a) the insolvent person has acted, and is acting, in good faith and with due diligence;
>
> (b) the insolvent person would likely be able to make a viable proposal if the extension being applied for were granted; and
>
> (c) no creditor would be materially prejudiced if the extension being applied for were granted.

5 The parties agree that this is the law that governs the motion before the Court. They also agree that Entegrity bears the burden of proof to satisfy each of the three parts of the test. If Entegrity fails to satisfy the Court on any of the three branches of the test, then its motion must fail. (See *Baldwin Valley Investors Inc., Re*, 1994 CarswellOnt 253 (Ont. Gen. Div. [Commercial List]) at para. 7). Entegrity met all three branches of the test in its initial application for an extension of time, but each of those three branches must be now revisited to determine whether Entegrity continues to meet its legal requirements for a further extension as its efforts since August 19, 2009 may demonstrate.

***1. Has Entegrity acted in good faith and with due diligence?***

6 In addition to the affidavit evidence presented on the application for the initial extension, Entegrity relies on the affidavit of James Heath who is the President and Chief Executive Officer of Entegrity, and also owns or controls approximately 60% of all issued and outstanding shares in that company. Heath's affidavit was sworn on the 24th day of September, 2009. Entegrity also relies on the additional affidavit of Walter MacKinnon of Pricewaterhousecoopers Inc. as trustee for Entegrity, which affidavit was also sworn on the 24th day of September, 2009.

7 While continuing to rely on the affidavit evidence filed in opposition to the original application, Mercantile filed two additional affidavits: (1) that of John Gundy, Vice-President Commercial Lending and Portfolio Management for Mercantile, sworn on the 29th day of September, 2009; and (2) that of Robert W. Powell, Vice-President of A.C. Poirier and Associates, Inc., trustee in bankruptcy, sworn on the 29th day of September, 2009. In contrast to the application for the initial extension of time, where there was no cross-examination on the affidavits, all four of these named individuals were cross-examined on the 6th day of October, 2009. The transcripts of those cross-examinations form part of the evidence on this motion. Although the cross-examinations were conducted just a few days before the hearing of the motion, I was provided with transcripts of them and had the opportunity to review that evidence before the hearing.

8 Counsel for Entegrity urges that I consider this motion for an extension of time in the context of what was going on chronologically since the issuance of my last order, and given the happening of those events that I treat this motion as really an initial application and not an extension. Counsel outlined the chronology commencing with Mercantile's early enforcement of its security on July 9, 2009 through to the end of the initial extension on September 28, 2009 with the additional reference to the cross-examination on the affidavits which took place subsequent to that date. Counsel referred to a number of things which took place prior to the hearing before me on August 14, 2009, much of which I took into account in granting my order of August 19, 2009. She then went on to point out that A.C. Poirier turned over the keys to Entegrity's rented premises on August 18, 2009. This followed a decision of Taylor, J on August 14, 2009 where he dismissed Mercantile's motion to appoint a receiver and manager until the trial of the action by Mercantile against Entegrity (See *Mercantile Finance Services Ltd. v. Entegrity Wind Systems Inc.*, 2009 PESC 23 (P.E.I. S.C.)).

9 Counsel noted there was a dispute over who was responsible for the rent of Entegrity's Island premises between the time A.C. Poirier was in possession and the subsequent order by Taylor, J. There was also an issue after my earlier decision with respect to Entegrity's request to A.C. Poirier that it notify Entegrity's creditors of Taylor, J's decision. While these disagreements continued, Heath met with representatives of the Prince Edward Island Business Development Inc. ("BDI") on September 7, 2009, requesting additional funding in the amount of $350,000. On September 10, 2009, Entegrity paid the rental arrears, thus bringing interim closure to that issue. Finally, on September 24, 2009, BDI denied Entegrity's application for further funding.

10 Entegrity refers to these events in support of its position that it has been busy trying to attend to development of its proposal since August 19, 2009, but in much the same fashion as occurred in its initial 30-day period, it found itself in time-consuming disagreements with Mercantile. It argues this had the effect of detracting from the time granted in the last order to develop its proposal and therefore in effect put it back in the position it found itself during the initial 30-day period. Hence Entegrity argues it is really looking for its initial extension all over again and not a further extension to file its proposal.

11 While this argument is thoughtful, it is not persuasive. First of all many of the activities which Entegrity argues distracted it during the period August 19, 2009 to the date of this hearing, do not advance its position. For example, the dispute over the rent was not something which required the attention given it in light of Entegrity's primary goal of developing a proposal. More telling is the issue with respect to Entegrity's application to BDI. While it may be that making such an application was a demonstration of Entegrity's good faith in pulling together its proposal, the fact that Heath did not meet with representatives of BDI until September 7, 2009 shows a lack of due diligence. In saying this I am well aware that the evidence discloses Heath was in verbal contact with BDI prior to September 7, but he did not

actually meet with them until that date. His reason for not meeting with BDI for several weeks after I granted the 45-day extension is that he was too busy. The following appears at p. 9 of the transcript of October 6, 2009:

> Q. Mr. Heath, why is it that Entegrity filed its Notice of Intention to Make a Proposal on July 15th but you didn't bother to meet with PEI Development Inc. seeking funding until the week of September 7th?
>
> A. My schedule didn't allow it.
>
> Q. You're busy?
>
> A. Yes.
>
> Q. Too busy?
>
> A. Too busy.

12 Whether Heath has other business ventures that preoccupied him or not, I do not know, but having applied for, and obtained, an initial extension to file its proposal, the actions of its Chief Executive Officer, or perhaps his inactions, do not support a finding of due diligence. To the contrary, one might have thought Heath would be on BDI's doorstep immediately after the order for extension of time on August 19, 2009, rather than waiting as he did until September 7, only to find out his application was denied on September 24, 2009. In my view, this delay is more indicative of a lack of importance in getting on with development of a proposal, which would include additional financing, than it does with meeting the test of due diligence.

13 What was Heath doing during the initial extension period? His evidence is that he was working 12 to 16 hours a day on this file. If that is so, he certainly did not reap the benefits of those long hours. As will be seen under the second branch of this test, he has been in discussion with two marketing companies, but no additional investors have been identified.

14 Entegrity's trustee, Walter MacKinnon, offers his professional opinion that Entegrity has acted in good faith and with due diligence with respect to restructuring in order to complete preparation of its proposal. He offers his reason for that statement in para. 3 of his affidavit citing as support the fact Entegrity made application to BDI for interim financing; that Heath took care of the rental arrears for both PEI locations; that Heath committed $75,000 of his own money to the company; that Entegrity reduced its overhead costs; and that during the initial extension period Entegrity secured some new orders, completed warranty work and offered immediate plans to commence production to fill the orders. However the basis for MacKinnon's opinion is information provided to him by Heath. That being so, if Heath's evidence is undermined in any significant way, then MacKinnon's opinion on due diligence is of little value. There is nothing in the evidence to suggest that MacKinnon checked out or verified what Heath was telling him.

15 It appears during the extension period Heath was able to obtain four new orders, but his work force has been reduced to approximately ten individuals — two in Prince Edward Island and eight in the United States. One might expect if Entegrity was acting in good faith and with due diligence, that there would be some signposts pointing in the direction of additional investors in the company. A name which surfaced in the initial application and comes up again is that of Valmont Industries. At para.37 of his affidavit, Heath states that Valmont continues to be a potential equity investor and remains interested "but is reluctant to provide a commitment in writing". Heath confirmed in his cross-examination that Valmont was aware if the present extension is not granted then Entegrity would be bankrupt, but still it would not provide any commitment in writing. What Entegrity has from Valmont is nothing.

16 At paras. 35 and 36 of his affidavit, Heath speaks about two companies. The first is Pure Energy Professionals Ltd. which is not an investor but some sort of marketing company. Attached to Heath's affidavit as Exhibit M is a copy of a letter dated September 23, 2009 from Pure Energy to Heath in which appears in the first paragraph the following:

> Subject to the successful continuation of Entegrity Wind Systems Inc. (EWSI) beyond its extension hearing on September 28, 2009, Pure Energy Professionals Ltd. (PEP) has a sincere interest in continuing its discussions toward the development of a joint venture between our companies, as outlined in our proposal of May, 2009 (attached).

The best Pure Energy can offer is "a sincere interest in continuing its discussions" with Entegrity. Likewise, attached as Exhibit N to Heath's affidavit is a copy of letter from Western Community Energy to Entegrity dated September 22, 2009. That letter reads in part:

> Subject to the successful continuation of Entegrity Wind Systems Inc. (EWSI) beyond its BIA extension hearing on September 28, 2009, Western Community Energy (WCE) has a strong interest in continuing its discussions with EWSI...; however, we are both awaiting clarification of the legal status of EWSI before proceeding further.

Western Community Energy is not an investor. The best it can offer is "a strong interest in continuing its discussions with EWSI".

17 Entegrity argues that the contact with Pure Energy and Western Community Energy are indicative of the progress it is making. It says it needs these marketing tools in order to set Entegrity up as a viable company worthy of investment. In the long run, that may be correct, but presently, Entegrity needs money. None of these three companies mentioned are willing to invest a nickle in Entegrity. They are willing to continue discussions but with no foreseeable goal in sight.

18 In my view, Entegrity has attempted to recast its argument on good faith and due diligence that carried it through the day in its original application. At that time, Entegrity argued successfully that it was being impeded by the actions of Mercantile from the time it filed its Notice of Intention to Make a Proposal, and in addition, it floated the name of Valmont Industries as one target which it felt would invest in the company but more time was needed to bring that to fruition. At the August 14 hearing, Mercantile argued that there was no substance to those discussions between Heath and Valmont; the nature and extent of any involvement proposed by Valmont were missing; whether Valmont's interest included a provision for paying out Mercantile or indeed any terms and conditions of Valmont's interest. Mercantile argued at that time, unsuccessfully, that the reference to Valmont was nothing more than a bare assertion.

19 It is now October, 2009, and we have nothing more from Valmont, not even an indication in writing that they are interested in Entegrity. Add to that the reference to Pure Energy and to Western Community Energy, and in my view all you have is pure fluff. There is no substance here. Entegrity has failed to meet the first part of the test. In my view it has not acted in good faith and with due diligence. On that basis alone, its motion for an extension of time ought to be dismissed. However, for completeness I shall now proceed to deal with the second and third parts of the test to determine whether Entegrity might be successful on either or both of those branches.

***2. Would Entegrity likely be able to make a viable proposal if the extension being applied for were granted?***

20 In the *Baldwin Valley* case at para. 4, Farley J. discussed a viable proposal as contemplated by the second branch of the test as follows:

> 4 It seems to me that "viable proposal" should have to take on some meaning akin to one that seems reasonable on its face to the "reasonable creditor"; this ignores the possible idiosyncrasies of any specific creditor. However, it does appear to me that the draft proposal being floated by the debtor companies is one which proposes making the Bank (which has lost faith with the management of the debtor companies) a partner with the owners of the debtor companies, failing which (a likely certainty in these circumstances) the debtor companies propose that third parties become equity participants instead of the Bank; yet there is no indication of the names and substance of these fallback partners. It does not appear to me that the debtor companies have shown that they are likely to be able to make a viable proposal. While that need not be a certainty: see my views at pp. 10 - 11 in Re Cumberland Trading Inc. released January 2, 199. "Likely" as defined in the Concise Oxford Dictionary of Current English, 7th ed. (1987; Oxford, The Claredon Press) means: *likely* 1. such as *might well happen*, or turn

> out to be the thing specified, *probable* 2. to be *reasonably expected* [emphasis added] I do not see the conjecture of the debtor companies' rough submission as being "*likely*".

Unlike the case before Farley J., I do not have a draft proposal to consider. There are no new investors prepared to commit any infusion of capital to Entegrity at this point in time, so how can Entegrity hope to advance a viable proposal?

21 Entegrity argues that its cash flow statement will do the trick. At para. 21 of his affidavit, Heath states:

> The Cash Flow Statement for all intents and purposes will be substantially what is used to formulate the Proposal.

That cash flow statement, it is argued, demonstrates that Entegrity is well on its way to developing a viable proposal. I disagree for two reasons:

> (1) The cash flow statement which is attached to Heath's affidavit as Exhibit L includes cash from the bank in the amount of $300,000. It is clear from Heath's affidavit and subsequent cross-examination, that this $300,000 refers to the $350,000 he sought to borrow from BDI and was denied.
>
> (2) The cash flow statement includes under the heading "Miscellaneous In-flows" the sum of $10,000,000. This is the equity investment Heath intends to raise. He has not done so. There is no $10,000,000.

Although Entegrity argued that even backing these two items out of its cash flow statement it is still showing growth based on completion of eleven backlog orders (See Heath's affidavit, Exhibit P) and four new orders, I am not convinced that is the case. Rather, it appears Entegrity has included two significant items in its cash flow statement which are essential on a go-forward basis. In fact, Entegrity has neither of these cash infusions in place.

22 As was the case on the issue of due diligence, MacKinnon's affidavit supports the cash flow statement as an indicator that a viable proposal is likely. However, there is no evidence that he verified the calculations in that cash flow statement and certainly in para. 4 of his affidavit he makes no reference to the fact that the $10,000,000 is not in place. Therefore, MacKinnon's affidavit is of little support to Entegrity.

23 In contrast, Robert Powell deposes at para. 32 of his affidavit as follows:

> 32. Upon my review of Mr. Heath's Affidavit and Mr. MacKinnon's Affidavit, and based upon my knowledge of the company's operations, cash flow, and financing, I have significant concern regarding EWSI's ability to put forward a viable proposal because of the following, which is not intended to be exhaustive:
>
> a. Aside from Mr. Heath's assertion that funds will be available to finance the company's operations through the further extension period, there is no evidence of sufficient receipts or capital to do so.
>
> b. EWSI has drastically reduced its workforce and appears to have only one employee in each of the Charlottetown and Albany locations (though such employees have not been identified). Based upon my understanding of the operations of the company, it is impossible for EWSI to meet its cash flow projections with one employee in each of its production facilities in PEI;
>
> c. EWSI has not put forward any evidence that its key suppliers and creditors, such as Wilson Manufacturing, are prepared to support EWSI's efforts to restructure and whether they will continue to supply EWSI during the further extension period;
>
> d. Mr. Heath has deposed that EWSI obtained four new orders for wind turbines, but there is no evidence that these sales are being made on a profitable basis. Without evidence to the contrary and given EWSI's recent material losses and the fact that manufacturing employees have not been retained, it is extremely unlikely that these sales could be made on a profitable basis.

e. The evidence put forward does not support the conclusion that EWSI's employees (who have not been paid since mid May 2009) will be paid their back wages and would continue to work for the company during the extension period or otherwise;

f. It appears that EWSI's operations and employees are now primarily located in the United States.

Paragraph 32 provided some detail in support of Powell's statements at para. 5 where he offered the following:

> 5. I have read the Affidavits of James Heath and J. Walter MacKinnon, C.A., both dated September 24, 2009, in support of EWSI's motion for a further extension of time in which to file a proposal. It is my professional opinion after reviewing those Affidavits, and in particular the Cash Flows and other supporting documentation attached to the Affidavit of Mr. Heath, that EWSI has not established that it will be able to make a viable proposal if the further extension sought by EWSI is granted, or at all. I address specific concerns and deficiencies in EWSI's Cash Flow Statement and supporting materials below.

24 Powell was cross-examined on his professional opinion that Entegrity has not established that it will be able to make a viable proposal. This cross-examination appears at p. 57 of the transcript commencing at line 11, and continuing on p. 58 as follows:

> Q. You come to the conclusion that it's your professional opinion that Entegrity ". . . has not established that it will be able to make a viable proposal. . ."
>
> A. Yes.
>
> Q. For purposes of that statement, "make a viable proposal", are you addressing this as, from the perspective of Mercantile?
>
> A. No.
>
> Q. No? Explain to me, then, this statement that you're making.
>
> A. Well, the company has not proven that it has any ability to obtain equity capital to finance a proposal. It's got no demonstrated access to working capital to even operate the business, and has laid off all of its employees, or substantially all of its employees with no apparent prospect of them coming back, based on the cash flows and materials filed by Mr. Heath.
>
> Q. Unless Mr. Heath obtains this equity investor.
>
> A. But, there's no evidence to that, and so I can only go with what evidence he's put forward —
>
> q. Right, but when you're —
>
> A. — in making my conclusion.
>
> Q. Okay. So a viable proposal, you're saying, is broad spectrum and not related to your role with Mercantile?
>
> A. No, it's with respect to all creditors.

25 The evidence before me supports the conclusion that Powell reviewed and analysed all the financial information relied on by Entegrity, including its centrepiece, the cash flow statement. I prefer Powell's evidence here over that of MacKinnon because Powell critically analysed the data provided by Entegrity, while MacKinnon merely relied on Heath and did no analysis of his own.

26 Not only does Entegrity lack any new investors for its venture, it has suffered substantial losses which have culminated in its insolvency. For the twelve-month period ending December 31, 2008, Entegrity incurred a loss of $6,463,850. For the five-month period ending May 31, 2009, Entegrity incurred a further loss of $1,884,000. Since the commencement of its operations in the fall of 2004, Entegrity has accumulated net losses of $12,873,689. Given this history, the lack of any new investor in sight, and the apparent substantial deficiencies in the cash flow statement, which is at the centre of its proposal, it does not appear to me that Entegrity has shown that it is likely to be able to make a viable proposal. Therefore, Entegrity fails on the second branch of the test.

***3. Will any creditor be materially prejudiced if the extension being applied for were granted?***

27 In its argument, Entegrity underlined the fact that it is "material" prejudice which is at issue here, not just any prejudice to a creditor. I agree. Mercantile is the only creditor opposing the extension and Entegrity points out that Mercantile holds extensive security over the assets of Entegrity. It relies on the case of *Nortec Colour Graphics Inc., Re* (2000), 18 C.B.R. (4th) 84 (Ont. Bktcy.) for the proposition that a creditor like Mercantile who opposes a request for an extension on the basis of material prejudice is required to quantify its losses and give particulars of prospective purchasers for its equipment.

28 Counsel for Entegrity notes that in her cross-examination of John Gundy, he asserts he has had an expression of interest in the company, but refuses to provide details. She also points to another area of his cross-examination where he indicates he is not aware of the present status of Entegrity and he has not made any inquiries of the company with respect to same. In summary, Entegrity argues Mercantile cannot maintain it will suffer material prejudice if the extension of time to file a proposal is granted when a senior officer in Mercantile is not aware of Entegrity's present status and has made no inquiries about its security.

29 At p. 41 of the transcript of his cross-examination, Gundy is asked:

> Q. Do you consider Mercantile to be in its worst case scenario now?
>
> A. I'd consider, at the moment, it is. If it goes any further, it's simply digging deeper into a hole.

That answer appears to suggest that Mercantile's position cannot get any worse. However, at p. 45 the following question and answer appear:

> Q. You have already indicated, though, as far as you're concerned, Mercantile has kind of bottomed out, it's worst case position right?
>
> A. I think the position continue, can continue to get worse for Mercantile and for the company.

On the one hand, Gundy says it can't get any worse and then a little later on in his testimony he indicates Mercantile's position can deteriorate further.

30 Entegrity relies on the case of *Cantrail Coach Lines Ltd., Re*, 2005 BCSC 351 (B.C. Master) at para. 22 where Master Groves for the British Columbia Supreme Court concludes:

> ...There is no evidence of substantial prejudice or considerable prejudice. There is no evidence that in not being allowed to realize their security at this time that there is, for example reduced security or, for example, that there are buyers out there for these assets they wish to seize under their security who will not be around once the proposal has had its opportunity to succeed or fail, once it has been completely formulated and presented to creditors. . . .

31 Mercantile responds to this reference in a variety of ways. In particular, Mercantile refers to Exhibit A to the most recent affidavit of Gundy where appears a copy of a letter dated September 15, 2009 to James Heath from Owens Community College, alleging a breach in the delivery, installation, technical support, commissioning and five-year

operating and maintenance agreement for the purchase of one of Entegrity's wind turbine systems. The letter suggests that Owens Community College has been in contact with Heath as early as May, 2009; that Heath did not deny the breach of contract; but as of September 15, 2009, the breaches complained of have not been remedied. In its submissions, Entegrity did not take issue with this letter and although I am cognizant of the fact that these are allegations only, it does point to a situation where a customer of Entegrity is not satisfied with the system or its maintenance and this in turn might have some bearing on Mercantile's overall security. The letter is certainly not an indicator that things are going in a positive direction for Entegrity.

32 Mercantile submits material prejudice will befall it if the extension is granted based on its belief that the only hope for Entegrity is that it be sold as a going concern. As time passes, this option becomes more remote simply because the majority of the work force is gone and it is not known whether they will return. In fact seven judgments have already been entered against Entegrity by the Inspector of Labour Standards for the Province of Prince Edward Island for wages owed to employees.

33 Further, Mercantile argues that some of its security is going out the door without it having any recourse because it is powerless to intervene while Entegrity develops its proposal. It argues that if Entegrity is bankrupt, then the trustee takes control of the assets of the company and attempts to put it in a viable position. Mercantile offers Powell's evidence at para. 35 of his affidavit as proof of material prejudice. It is worthy of reproduction here:

> 35. I believe that the granting of a further extension as requested by EWSI will further prejudice MFSL. In my view, the highest value for MFSL collateral is by sale as a going-concern and that value is rapidly eroding as time passes for the following reasons:
>
> a. EWSI had approximately 55 employees in May, 2009, when EWSI ceased paying them. EWSI has just started paying only 8 of those employees starting in September 2009. As more time passes, the likelihood that skilled manufacturing and service employees find other jobs increases thereby increasing the risks and costs associated with re-starting production.
>
> b. EWSI appears to have done fairly little in terms of servicing customers since well prior to the filing of the Notice of Intention to Make a Proposal. All that appears to have been done is warranty work on 23 machines and the completion of the installation of 4 machines. However, there does not appear to be any revenue from this work reflected in the actual receipts and disbursements to date nor in the projection. Also, it is noted that EWSI has failed to complete a contract with Owens Community College, who made a payment to EWSI of U.S. $73,000 on July 9, 2009, just prior to the filing. Owens has now noted EWSI in breach of the contract. It appears that EWSI's reduced workforce and lack of working capital is jeopardizing customer contacts and relationships and thereby damaging the going-concern value of EWSI's assets.
>
> c. In addition, I am concerned that the weak state of EWSI and the lengthy period of time that they are taking to formulate a proposal will cause customers to abandon EWSI in search of alternative suppliers. Again, this will damage the going-concern value of EWSI's assets.
>
> d. EWSI, prior to filing, had contracted with a supplier in Quebec to manufacture new molds for the production of the wind turbine blades. These would appear to be critical to the future manufacturing capability of EWSI as I understand that the existing molds are near the end of their useful life. I understand that the supplier has manufactured the molds and is seeking payment of approximately $60,000 for the release of the molds. Mr. Heath has not addressed this situation and it appears that the payment of the $60,000 is not incorporated into the cash flow projection. The loss of these molds could have a negative impact on the ability to obtain going-concern value for EWSI's assets.

I find Powell's assertion here to be credible and reliable and based, in large part, on information provided by Entegrity.

34 At para. 22 of his factum, counsel for Mercantile sets out the factors upon which he bases his conclusion that Entegrity will be materially prejudiced if the extension sought is granted. The following appears at para. 22:

> 22. MFS submits that it, as well as other creditors (including EWSI's employees), will be materially prejudiced if the extension sought is granted. MFS's position is premised on the following factors:
>
> a. EWSI has been in default of its obligations to MFS since May of 2009, and the total secured indebtedness to MFS as at July 9, 2009 was in excess of $3 million, with a per diem since that time of over $1,880;
>
> b. each day that passes erodes MFS's security, and the total indebtedness continues to rise;
>
> c. no employees of EWSI have been paid since mid-May of 2009, and the passage of time renders the possibility of salvaging EWSI's operations more remote.
>
> d. MFS has lost all confidence in the ability of James Heath to manage EWSI's affairs and business operations;
>
> e. if EWSI is deemed to have made an assignment in bankruptcy, all of the assets of EWSI will vest in its Trustee in Bankruptcy, thereby preserving those assets, and the Trustee has the power to operate the company, under the oversight of the Court;
>
> f. EWSI has offered no evidence in the Affidavits submitted on its application for a second extension of time as to how it would mitigate or avoid any material prejudice to creditors. The issue of material prejudice is simply not addressed in any substantive way in the Affidavit evidence put forward by EWSI on this application;
>
> g. EWSI had approximately 55 employees in May 2009, when EWSI ceased paying them. EWSI now, according to the evidence of Mr. Heath, has two or perhaps three employees in Prince Edward Island who may be receiving current pay. However, as more time passes, the likelihood that skilled manufacturing and service employees will find other jobs increases, thereby increasing the difficulties and costs associated with restarting production;
>
> h. as noted by Robert Powell in his Affidavit at paragraph 35, there does not appear to be any revenue received by EWSI for warranty work, or in the installation of four machines. Further, EWSI has failed to complete a contract with Owens Community College, who made a payment to EWSI of U.S. $73,000 on July 9, 2009. Mr. Powell concludes that EWSI's "reduced workforce and lack of working capital is jeopardizing customer contracts and relationships and thereby damaging the going concern value of EWSI's assets";
>
> i. also in paragraph 35 of his Affidavit, Mr. Powell deposes that "I am concerned that the weak state of EWSI and the lengthy period of time that they are taking to formulate a proposal will cause customers to abandon EWSI in search of alternative suppliers. Again, this will damage the going concern value of EWSI's assets";
>
> j. as stated by Mr. Gundy in his Affidavit at paragraph 24,
>
> > EWSI is an insolvent company that has lost substantially all of its workforce; is faced with substantial warranty claims; lacks the necessary operating funds to carry on any meaningful business; is in breach of its obligations to past customers; and lacks the credibility required to attract new customers. It becomes more and more unlikely as every day goes by that EWSI can be turned around and sold on anything approaching a going concern basis to provide for any meaningful recovery by creditors. I believe we are very quickly reaching the point where there will be no hope for any such recovery.

> As a result, I believe MFS and all other creditors will suffer very significant material prejudice if a further extension is granted.
>
> [Emphasis added]

The evidence before me supports the statements contained in clauses (a), (b) and (c) of paragraph 22. As for clause (d), loss of confidence in James Heath is not conclusive of the matter. Clause (e) is correct, and I agree with the statement contained in clause (f). As for clause (g), the number of employees referenced there is substantially correct according to the evidence of Mr. Heath and with that I agree. The suggestion that the skilled manufacturing and service employees will not likely return to their jobs unless something is done very soon, is to a certain extent, conjecture, but may be a logical conclusion to be drawn from the present state of affairs. Clauses (h) and (i) reference facts which are a cause for concern that may result in material prejudice to Mercantile. Finally, clause (j) refers to the evidence of Gundy which is factually correct except for the underlined portion which represents his opinion.

35 The question I must ask myself is whether it is more likely than not that Mercantile will suffer material prejudice if the requested extension is granted? After considering the arguments advanced by both parties, I am of the view Mercantile would suffer material prejudice and therefore Entegrity has failed to satisfy this third branch of the test. This material prejudice exhibits itself not simply in the amount which is currently owed by Entegrity to Mercantile and the per diem that continues to pile up since Entegrity's default, but it is the accumulation of all those other factors referred to by Mercantile which would further erode its position if the extension were granted. I am thinking of such things as the reduced workforce and the uncertainty as to their return; Entegrity's completion of warranty work without any profit associated therewith; complaints from customers who are unsatisfied with the product or service associated with the product, which if allowed to continue will further undermine the customer base and make it more difficult for the company to be turned around so that Mercantile's exposure can be eliminated or reduced. These are but examples. There are others.

36 For all of the foregoing reasons I conclude Entegrity has failed to discharge the onus on it as set out in s-s. 50.4(9) of the Act. It has failed to satisfy me on each of the three branches of the test set out in that subsection, and therefore I am unable to exercise my discretion to grant the extension requested. Mercantile shall have its costs in the cause against Entegrity which I expect will offset the costs awarded to Entegrity in my decision of August 19,2009.

**End of Document**



 

TAB 4

1994 CarswellOnt 253
Ontario Court of Justice (General Division [Commercial List]), In Bankruptcy

Baldwin Valley Investors Inc., Re

1994 CarswellOnt 253, [1994] O.J. No. 271, 23 C.B.R. (3d) 219

# Re proposal of BALDWIN VALLEY INVESTORS INC. and of VARION INCORPORATED

Farley J.

Judgment: February 3, 1994 *
Docket: Doc. 32-65038

Counsel: *Frank Bennett* , for debtor companies.
*Larry Crozier* , for secured creditor, Royal Bank of Canada.

Subject: Corporate and Commercial; Insolvency
**Related Abridgment Classifications**
Bankruptcy and insolvency
VI Proposal
VI.2 Time period to file
VI.2.a Extension of time
**Table of Authorities**
**Cases considered:**
*Cumberland Trading Inc., Re* (1994), 23 C.B.R. (2d) 225 (Ont. Gen. Div. [Commercial List]) — *referred to*
**Statutes considered:**
Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 —

s. 50.4(9)

s. 50.4(11)

Appeal from decision of Registrar in Bankruptcy [reported at 23 C.B.R. (3d) 219 at 223 ] dismissing second application for extension of time to file proposal under *Bankruptcy and Insolvency Act* .

***Farley J.:***

1 Baldwin Valley Investors Inc. ("Baldwin") and Varion Incorporated ("Varion"), the debtor companies appealed the dismissal of their extension of time to file proposals requests heard January 27, 1994 by Registrar Ferron. The Registrar indicated that he had refused extensions that day with reasons to follow shortly [reported at 23 C.B.R. (3d) 219 at 223 ]. The matter came before me on January 28th and on consent was adjourned to be heard today when it was expected that reasons would be available, as they in fact were. The Registrar was of the view that the debtor companies had failed to meet all three tests under s. 50.4(9) of the *Bankruptcy and Insolvency Act* , R.S.C. 1985, c. B-3 as amended ("BIA"). That section provides that:

> (9) The insolvent person may, before the expiration of the thirty day period mentioned in subsection (8) or any extension thereof granted under this subsection, apply to the court for an extension, or further extension, as the case may be, of that period, and the court may grant such extensions, not exceeding forty-five days for any individual

extension and not exceeding in the aggregate five months after the expiration of the thirty day period mentioned in subsection (8), if satisfied on each application that

(*a*) the insolvent person has acted, and is acting, in good faith and with due diligence;

(*b*) the insolvent person would likely be able to make a viable proposal if the extension being applied for were granted; and

(*c*) no creditor would be materially prejudiced if the extension being applied for were granted.

This should be contrasted with the termination provisions of s. 50.4(11) which provide that:

(11) The court may, on application by the trustee, the interim receiver, if any, appointed under section 47.1, or a creditor, declare terminated, before its actual expiration, the thirty day period mentioned in subsection (8) or any extension thereof granted under subsection (9) if the court is satisfied that

(*a*) the insolvent person has not acted, or is not acting, in good faith and with due diligence,

(*b*) the insolvent person will not likely be able to make a viable proposal before the expiration of the period in question.

(*c*) the insolvent person will not likely be able to make a proposal, before the expiration of the period in question, that will be accepted by the creditors, or

(*d*) the creditors as a whole would be materially prejudiced were the application under this subsection rejected,

and where the court declares the period in question terminated, paragraphs (8)(*a*) to (*c*) thereupon apply as if that period expired.

2 The facts are as set out in the Registrar's reasons released today. Counsel were agreed that the standard of review was that I had to be satisfied that the Registrar either erred in law or in principle.

3 Let me deal with the middle test of s. 50.4(9)(*b*) that the debtor companies must show that they "would likely be able to make a viable proposal if the extension being applied for were granted". The Registrar appeared to focus on the fact that the Bank, as the 92% creditor of Baldwin and almost 100% creditor of Varion, had lost all confidence in the debtor companies and would not vote for any proposal put forth. However, in my view this is not the test of s. 50.4(9)(*b*). This becomes clear when one examines s. 50.4(11)(*b*) and (*c*); it appears that Parliament wished to distinguish between a situation of a viable proposal (s. 50.4(9)(*b*) and (11)(*b*)) versus a situation in which it is likely that the creditors will not vote for this proposal, no matter how viable that proposal (s. 50.4(11)(*c*) but with no corresponding clause in s. 50.4(9)).

4 It seems to me that "viable proposal" should have to take on some meaning akin to one that seems reasonable on its face to the "reasonable creditor"; this ignores the possible idiosyncrasies of any specific creditor. However, it does appear to me that the draft proposal being floated by the debtor companies is one which proposes making the Bank (which has lost faith with the management of the debtor companies) a partner with the owners of the debtor companies, failing which (a likely certainty in these circumstances) the debtor companies propose that third parties become equity participants instead of the Bank; yet there is no indication of the names and substance of these fallback partners. It does not appear to me that the debtor companies have shown that they are likely to be able to make a viable proposal. While that need not be a certainty: see my views at pp. 10-11 in *Re Cumberland Trading Inc.* released January 24, 1994 [now reported at 23 C.B.R. (3d) 225, at p. 231]. "Likely" as defined in *The Concise Oxford Dictionary of Current English*, 7th ed. (1987; Oxford, The Claredon Press) means:

*likely* 1. such as *might well happen*, or turn out to be the thing specified; *probable*. 2. to be *reasonably expected*. [emphasis added]

I do not see the conjecture of the debtor companies' rough submission as being "*likely* ".

5 While one may well fault the Bank for its approach to this situation, one has to recognize that the onus is on the debtor companies to show that they have acted in good faith and with due diligence. I am satisfied that the Registrar correctly assessed the situation in that regard that the debtor companies could have and should have proceeded with laying the foundation for their proposal and in fact building on that foundation rather than relying on anything that may be forthcoming from the Bank. In particular, see Cohn, *Good Faith and the Single Asset Debtor* (1988) 62 Am. Bankr. L.J. 131 on which it appears the Registrar relied. However, it is noted that there was no examination of the jurisprudential principles therein.

6 I discussed the question of material prejudice in *Cumberland, supra* , at pp. 11-13 [pp. 231-232]. The debtor companies have provided no information in that regard for the 45 day extension period from February 28, 1994. The only information close to this is the cash-flow statement of the previous extension granted December 16, 1993. However, for this extension there was no information. It appears therefore, that the debtor companies did not even attempt to meet this condition.

7 I am therefore, of the view that on all three tests (one failure of a test being sufficient to disqualify a debtor company from being able to ask for an extension) the debtor companies have failed to overcome the onus on them. The Registrar was correct in the result on all counts, although I feel that he inadvertently used the wrong test in s. 50.4(9)(*b* ), a quite understandable situation given the terminology used in the legislation.

8 I would also point out that it was clear that if the debtor companies had won a victory in this appeal, it would have been a Pyhrric victory. The Bank would have been able to come right back in with a motion based on s. 50.4(11)(*c* ).

9 The appeal is dismissed. Costs were agreed at $2,500 and are payable by the debtor companies jointly and severally to the Bank forthwith.

*Appeal dismissed.*

Footnotes

* This judgment is an appeal from the decision reported at 23 C.B.R. (3d) 219 at 223 .

**End of Document**



 

TAB 5

2007 CarswellOnt 3796
Ontario Superior Court of Justice

Royalton Banquet & Convention Centre Ltd., Re

2007 CarswellOnt 3796, 33 C.B.R. (5th) 278

# Royalton Banquet and Convention Centre Ltd.

Reg. A.M. Diamond

Heard: June 11, 2007
Judgment: June 14, 2007
Docket: 31-959422

Counsel: Richard Jones for Proponent / Applicant
Emilio Bisceglia for Respondent, Creditor Westplex Centre Inc.

Subject: Insolvency
**Related Abridgment Classifications**
Bankruptcy and insolvency
VI Proposal
VI.2 Time period to file
VI.2.a Extension of time
**Table of Authorities**
**Cases considered by *Reg. A.M. Diamond*:**
*Benson v. Third Canadian General Investment Trust Ltd.* (1993), 1993 CarswellOnt 166, 14 O.R. (3d) 493, 13 B.L.R. (2d) 265 (Ont. Gen. Div. [Commercial List]) — considered
*Plancher Heritage Ltée / Heritage Flooring Ltd., Re* (2004), 2004 NBQB 168, 2004 CarswellNB 358, 3 C.B.R. (5th) 60 (N.B. Q.B.) — followed
**Statutes considered:**
*Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3
Generally — referred to

s. 50.4(1) [en. 1992, c. 27, s. 19] — referred to

s. 50.4(8) [en. 1992, c. 27, s. 19] — considered

s. 50.4(8)(a) [en. 1992, c. 27, s. 19] — referred to

s. 50.4(9) [en. 1992, c. 27, s. 19] — considered

s. 50.4(10) [en. 1992, c. 27, s. 19] — referred to

s. 135(4) — considered

s. 187(11) — referred to

s. 192 — referred to

s. 192(1)(j) — referred to

s. 192(1)(k) — referred to

APPLICATION by insolvent person for extension of time to file proposal.

***Reg. A.M. Diamond*:**

**Introduction**

1 The applicant seeks an extension of time to file a proposal under the *Bankruptcy and Insolvency Act* (BIA). On May 14, 2007 the applicant filed a Notice of Intention (NOI) to make a Proposal under section 50.4(1) of the BIA [1]. Pursuant to section 50.4 (8) of the BIA the debtor has 30 days from the date of filing its NOI to file a proposal or obtain an extension of time to file the proposal from the court. This matter was heard on June 11, 2007 on short service to the respondent despite the fact that the motion was booked with the court office on May 25, 2007.

**Preliminary Issues**

***Jurisdiction***

2 The jurisdiction of the Registrar in Bankruptcy is setout and limited to those powers setout in section 192 of the BIA. One of the things that a Registrar cannot hear, without consent of the parties, is an opposed application for a Division I Proposal. As this is an opposed application for an extension of time for filing such a proposal, which, if not granted would, under section 50.4 (8) (a) of the BIA result in the assignment of the debtor into bankruptcy, I think it is appropriate that I first address my authority to deal with the matter.

3 Section 192 (1) (k) of the BIA grants to the registrar in bankruptcy the power and jurisdiction to "hear and determine any matter relating to practice and procedure in the courts". I am of the view that the question of whether to grant additional time to file a proposal under the BIA and, if so, how much time to grant, is an issue dealing with "the practice and procedure of the bankruptcy court" and thus falls within my jurisdiction.

4 Second, section 192 (1) (j) grants to the registrar in bankruptcy the power and jurisdiction to "hear and determine any matter with the consent of all parties". Both parties were represented by experienced and competent counsel and both counsel had no reservations in my hearing and determining this issue.

***Timing***

5 Counsel for the applicant advised the court that it was urgent that I release my reasons by today as he and the trustee had calculated that the thirty days from filing the NOI expired at the end of June14, 2007 [2]. However, on reviewing the materials today it appears to me that the 30 days for filing their proposal expired at the end of the day yesterday, June 13, 2007. If I had been so advised I would have prepared these reasons before the expiry of the 30 days. The error is that of the applicant and the trustee.

6 This raises the question of whether, having brought the motion within the 30 days, the clock for the purposes of section 50.4 (8) is stopped or conversely is the applicant now out of time? Section 50.4 (8) reads:

> Where an insolvent person fails to comply with subsection (2), or where the trustee fails to file a proposal with the official receiver under subsection 62 (1) within a period of **thirty days** after the day the notice of intention was filed under subsection (1), or within any extension of that period granted under subsection (9).
>
> (a) the insolvent person is, **on expiration** of that period or that extension as the case may be, deemed to have thereupon made an assignment; (emphasis added)
>
> (b) ...

7 The wording of section 50.4(8) must be contrasted to the wording of section 135 (4) of the BIA, which reads:

> (4) A determination under subsection (1.1) or a disallowance referred to in subsection (2) is final and conclusive unless, within a thirty day period after the service of the notice referred to in subsection (3) or such further time as the court may on **application made within that period** allow, the person to whom the notice was provided appeals from the trustee's decision to the court in accordance with the General Rules. (emphasis added)

8 The general rule of statutory interpretation is that when parliament uses different language it intends different meanings. Section 135 (4) clearly contemplates the extension being granted after the expiry of the 30 days provided that the application for the extension was made within the 30 days. Section 50.4 (8) does not have the same saving language. Section 187 (11) grants to the court the power to "extend time either before of after the expiration thereof on such terms, if any, as it thinks fit to impose". However in subsection 50.4 (10) parliament specifically excluded the court from using this jurisdiction to extend the time under subsection 50.4 (9). The thirty days referenced in subsection 50.4 (9) is the same 30 days referenced in subsection 50.4(8), as result, I am of the view that I am specifically not empowered to extend the time past 30 days to allow for the filing of the proposal or the obtaining of an extension of that 30 days.

9 As a result I conclude that the applicant was deemed to have made and assignment in bankruptcy on June 13, 2007. It is not available to the applicant to file a proposal today. The applicant is bankrupt. Having said that, in the event that I am wrong with respect to the timing issue, I think it appropriate that I provide reasons as if the time did expire at the end of the day today.

**Background**

10 The respondent is the owner of a building designed and built to be used as a banquet hall. The applicant, is the respondent's tenant. There has been a lengthy history of disputes between the parties over the terms of the lease and in particular the applicant's duties to maintain the premises. This dispute culminated in a hearing before Mr. Justice Morawetz heard March 1, 2006. In short Morawetz J found for the respondent landlord. The respondent appealed and on April 5th 2007 the Court of Appeal dismissed the appeal. Based on the decision of the Court of Appeal and the applicant's alleged failure to comply with the order of Mr. Justice Morawetz the landlord brought a motion seeking *inter alia* termination of the lease. Before that motion could be heard the applicant filed its NOI.

11 The underlying cause of the disagreement between the applicant and the respondent is explained in paragraphs 2-4 of the reasons of Mr. Justice Morawetz where he finds that:

> [2] in January 2006, the principals of the [applicant] entered into an agreement, through a different corporation to acquire a second banquet hall, La Perla Banquet Hall, which is located a short distance away from the existing banquet hall that operates under the name of the applicant. When the [respondent] became aware of this acquisition plan, the [respondent]/[applicant] relationship changed dramatically.
>
> [3] The [respondent] became concerned that the [applicant] would be taking steps to abandon the leased premises and transferring the [applicant's] business to the newly acquired banquet hall. So far, notwithstanding a high degree of suspicion, there is no evidence to indicate that the [applicant] has been engaged in activity designed to transfer business from the existing banquet hall to the newly acquired banquet hall
>
> [4] The [respondent] reacted by requiring strict compliance with the provisions of the Lease.

12 On the hearing of this motion the respondent lead uncontroverted evidence that the applicant is now engaged in moving potential business from the hall owned by the respondent to a new hall which is owned and currently being renovated by a company controlled by the same principals as the applicant. The evidence is that all new bookings that are attempted to be made using the applicant's phone number for dates after the start of September are for the new company at the new location. As a result, as of September the applicant will not be able to be sold as a going concern as

it will have no bookings. Respondent's counsel submits that the applicant is using the courts and the bankruptcy system to simply "rag the puck" until their new place is available while at the same time running down the old location so that it will not be a competitor once they move.

**Analysis**

13 Section 50.4 (9) of the BIA reads in part:

> (9) The insolvent person may, before the expiration of the **thirty day period mentioned in subsection (8)** or any extension thereof granted under this subsection, apply to the court for an extension, or further extension, as the case may be, of that period, and the court may grant such extensions, not exceeding forty-five days for any individual extension and not exceeding in the aggregate five months after the **expiration of the thirty day period mentioned in subsection (8)**, if satisfied on each application that
>
> (a) the insolvent person has acted, and is acting, in good faith and with due diligence;
>
> (b) the insolvent person would likely be able to make a viable proposal if the extension being applied for were granted; and
>
> (c) no creditor would be materially prejudiced if the extension being applied for were granted. (emphasis added)

14 I agree with counsel for the respondent that in order to be granted an extension the applicant has the onus of demonstrating that it satisfies each of the three elements of the test. As found in *Plancher Heritage Ltée / Heritage Flooring Ltd., Re* (2004), 3 C.B.R. (5th) 60 (N.B. Q.B.)[3] "the debtor must prove on the balance of probabilities that an extension is justified...". I will deal with element of the test in turn.

***Good faith***

15 The evidence is that the applicant has, since at least January 2007, made some attempts to sell its business. The applicant's position as set out in its notice of motion it that:

> There are substantial outstanding disputes between [the applicant] and the respondent involving claims by the respondent that the applicant is required to make substantial expenditures on upgrading and refurbishing the premises. Those disputes must be resolved as part of any restructuring as a going concern of the business and undertaking of the applicant.

16 Counsel for the applicant conceded in oral submissions that it is impossible for the applicant and respondent to work together. Furthermore, as set out above, the uncontroverted evidence is that the principals of the applicant are in the process of moving all of its potential business to a new company at a new location. In light of this I cannot find that the applicant has satisfied the onus of demonstrating that it has acted in good faith with respect to making a proposal.

***Due diligence.***

17 As mentioned above the NOI was filed on May 14, 2007. At the end of the hearing I directly (over the objection of the respondent's counsel) asked the representative of the trustee what work had been done since May 14, 2007 in preparing the proposal. The trustee answered candidly and honestly that no work had been done on preparing the proposal. As a result I find that the applicant has not exercised the necessary due diligence to be granted an extension.

***Likelihood***

18 On its own material the applicant is deficient in this regard. In paragraph 11 of the affidavit of the president of the applicant he swears that the:

> [applicant] requires an extension of time to file its Proposal in order to continue efforts to resolve outstanding disputes and to determine the most advantageous terms for a restructuring and any possible related transactions. If [the applicant] is granted the extension, I am **hopeful** that [the applicant] will be able to make a viable proposal to its creditors within the extension period being sought. (emphasis added)

19 As I said at the hearing and as counsel agreed, being "hopeful" of winning the lottery is not the same thing as it being "likely". To quote Mr. Justice Farley in *Benson v. Third Canadian General Investment Trust Ltd.* [1993 CarswellOnt 166(Ont. Gen. Div. [Commercial List]) ] "If wishes were horses, then beggars will ride." There is no evidence before me that a proposal is likely. Counsel for the applicant conceded that based on the status of the relationship between the applicant and the respondent, the only type of proposal that is even conceivable at this time is a liquidation proposal. That is not what is implied by the applicant's affidavit, and as a result I find that the granting of the extension will not likely result in a viable proposal.

**Conclusion**

20 I am of the view that the 30-day period to file a proposal expired yesterday, June 13, 2007 and as a result the applicant is bankrupt as of today and unable to file a proposal. However, if I am wrong with respect to the calculation of the 30-day period then, as set out above, the granting of an extension of time to file a proposal is a matter of discretion. In exercising that discretion I find that the Applicant should not be granted an extension. The Applicant's motion for leave to extend the time for filing a proposal pursuant to section 50.4(9) of the BIA is denied.

*Application dismissed.*

Footnotes

1 See exhibit A to the moving party's affadavit

2 The trustee's belief that the 30 days expires on June 14, 2007 was confirmed by telephone message from the trustee to the court off today (June 14, 2007) in which the trustee advised court staff that if they required these reasons by 3:30 pm today.

3 As cited in *Houlden & Morawetz* at E 1.2

**End of Document**



 

TAB 6

longer than 45 days from the last with the total number of extensions not to exceed in the aggregate five months after the first 30-day period. Accordingly, the debtor has a total of six months to prepare the proposal following the filing of the notice of intention. These extensions give the debtor a reasonable time period to formulate a proposal while at the same time the creditors are protected as the debtor must return to the court for an order extending the time. In granting the extension, the court must be satisfied that:

(a) the insolvent person has acted in good faith and with due diligence;

(b) the insolvent person would likely be able to make a viable proposal if the extension were granted; and

(c) no creditor would be materially prejudiced if the extension were granted.[21]

There is no provision to extend the time beyond the six months.[22]

On the other hand, the trustee, an interim receiver if appointed, or any creditor may apply to the court for an order terminating the period of time to make a proposal.[23] The grounds upon which the court could terminate the period of time to make a proposal differ slightly from an application by the debtor for an extension of time to file a proposal pursuant to subsection 50.4(9).

## *Material Prejudice*

Most litigation focuses on the viability of the debtor's proposal and whether any creditor is "materially prejudiced". The insolvent person has the onus of proof in applying for an extension and, at that time, the insolvent person must demonstrate that the creditors will not be "materially prejudiced". This may be a difficult task for a debtor where the security of the secured creditor is diminishing, depreciating, or declining in value. For example, if the value of the security drops below the debt, the secured creditor can argue that its position is prejudiced. While the amendment contemplates that the secured creditor can be prejudiced, the court is confronted with the more difficult issue as to the extent of the prejudice. There are no statutory guidelines for this. In considering the degree of prejudice, the court reviews a number of factors in deciding whether creditors are materially prejudiced. These include, among others:

- the degree and speed of erosion of the assets — that is, how quickly the assets are being converted into cash and spent on operating and restructuring costs;

[21] Subsection 50.4(9).

[22] Subsection 50.4(10).

[23] Subsection 50.4(11).

- the type of asset — if the asset is real property, the erosion will likely be slow in a falling market; if the assets are accounts receivable and inventory, the erosion may be quicker, and in this case, the court will consider whether these assets are being replaced at sufficient levels to minimize the prejudice;
- the length of stay with respect to the extension — the court can grant an extension up to 45 days on each application for a total period of six months;
- the risk of the assets dissipating — the court reviews whether the assets are being sold at less than cost;
- the risk to the major secured creditors;
- whether new business is being generated;
- some qualitative analysis — that is, the ratio of assets to the debt at any given time; and
- the size of the restructuring costs in relation to the overall benefit to the creditors if the debtor is given the opportunity to prepare a proposal.

While the debtor may obtain an initial 10-day stay of proceedings from secured creditors, and perhaps longer, a secured creditor who holds substantially most of the debt will likely be successful in terminating the proposal process or in lifting the stay of proceedings to appoint a receiver if it wishes to exercise its rights. In view of the tests imposed on the debtor and the secured creditor, it is clear that secured creditors control the proposal process. However, the secured creditor has the onus of establishing that it is materially prejudiced if it wants to defeat the motion for an extension.

## *Effects on Filing*

On the filing of a notice of intention or on the filing of the proposal itself, there is a stay of proceedings with respect to the rights and remedies of all creditors for 30 days,[24] which, as indicated above, may be extended in 45-day periods. Often, a debtor is not able to formulate a proposal within the initial 30-day period where creditors are pressing for payment or are threatening to enforce their security. The notice of intention gives the debtor 30 days at a minimum to file a proposal while, at the same time, it stays the rights of creditors to continue or commence proceedings against the debtor. In addition, the stay operates to prevent anyone who is a party to an agreement with the insolvent person from terminating or amending the agreement or acceler-

[24] Subsection 69(1). However, in **Re Canadian Petcetera Ltd. Partnership** (2009), 55 C.B.R. (5th) 20 (B.C. C.A. [In Chambers]) the landlord denied the tenant debtor access to the premises after the tenant debtor filed a notice of intention to make a proposal. On an application for a mandatory injunction against the landlord, the court dismissed the application on the basis that the tenant would not suffer irreparable damages if the tenant lost only one of its stores, that applicant was not in a position to give an undertaking as to damages and the balance of convenience favoured the landlord.

**2018 01 22164**
**SUPREME COURT OF NEWFOUNDLAND AND LABRADOR**
**IN BANKRUPTCY AND INSOLVENCY**

**IN THE MATTER OF** the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended

**AND IN THE MATTER OF** the matter of the Proposal of Burry's Shipyard Inc.

Estate No. 51-2397788
Court No. 22164
District: Newfoundland & Labrador
Division No. 01-Newfoundland & Labrador

| **SUMMARY OF CURRENT DOCUMENT** | |
|---|---|
| Court File Number | 2018 01 22164 |
| Date of Filing Document | October 23, 2018 |
| Name of Party Filing or Person | Business Development Bank of Canada |
| Application to which Document being filed relates: | Application seeking an extension to the stay of proceedings granted by this Honourable Court pursuant to the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "**BIA**") |
| Statement of Purpose in filing: | To provide position of Business Development Bank of Canada on application |
| Court Sub-File Number, if any | |

## AFFIDAVIT

I, Allison Philpott, of the City of St. John's, in the Province of Newfoundland and Labrador, Barrister and Solicitor, make oath and say as follows:

1. That I am an associate in the law firm Cox & Palmer, solicitors for Business Development Bank of Canada ("**BDC**"), and have full knowledge of the matters herein deposed of, except where stated to be based upon information or belief.

2. That BDC is a senior secured creditor of BSI with current outstanding loans in the amount of $1,177,712. 24, which loans have been in arrears for a periods varying from two (2) to four (4) months.

3. That on October 19, 2018 I was informed by Robert Prince, Director of Business Restructuring with BDC, that he received an e-mail from Kurt Macleod, Manager of Financial Advisory Services with Deloitte Restructuring Inc., Proposal Trustee of Burry's Shipyard Inc. ("**BSI**"). The e-mail indicated that Mr. Macleod was skeptical that a viable option would be received in time to warrant another extension to the stay of proceedings and that, aside from the offer from Heddle Marine Inc., BSI did not have any other viable options at that time. A true copy of this e-mail correspondence is attached hereto as **Exhibit A.**

4. That on October 19, 2018 I was also informed by Robert Prince that he received an e-mail from Mr. Macleod stating that Heddle Marine Inc. had indicated that it would not be submitting a new offer to purchase the assets of BSI. A true copy of this e-mail correspondence is attached hereto as **Exhibit B**.

**SWORN/AFFIRMED** before me at the City of St. John's, in the Province of Newfoundland & Labrador, this 23 day of October, 2018.

A Commissioner for taking affidavits.

Allison Philpott

**ASHLEY TIPPETT**
A Commissioner for Oaths in and for
the Province of Newfoundland and Labrador.
My commission expires on December 31, 2022.

THIS IS EXHIBIT " A " TO
THE AFFIDAVIT OF
Allison Philpott
Sworn to before me
this 23 day of Oct , 2018
Ashley Tippett

**ASHLEY TIPPETT**
A Commissioner for Oaths in and for
he Province of Newfoundland and Labrador.
y commission expires on December 31, 2022.

## Philpott, Allison (St. John's)

**From:** Macleod, Kurt (CA - Halifax) <kmacleod@deloitte.ca>
**Sent:** Thursday, October 18, 2018 9:53 AM
**To:** PRINCE, Robert (MONCTON)
**Cc:** Jones, Neil X. (CA - Halifax)
**Subject:** RE:BSI

Good morning Bob,

Nothing yet. We do have an executed engagement letter with Spergel and another firm Vinecrest to source financing, however, I am sceptical that a viable option will be received in time to warrant an extension.

I am getting extremely frustrated with heddle and their disregard for deadlines. However, tactically the company does not have any other viable options at this time.

Regards,

Kurt

Sent from my iPhone

On Oct 18, 2018, at 9:16 AM, PRINCE, Robert (MONCTON) <robert.prince@bdc.ca> wrote:

> Good morning gentlemen,
>
> Is there any update from either Heddle or Spergel?
>
> **Robert (Bob) Prince**
> Director, Business Restructuring | Directeur, Restructuration d'entreprise
> T 506-851-7612 C 506-874-0863
>
> <image001.jpg>
>
> bdc.ca
>
> <image002.jpg> <image003.jpg> <image004.jpg> <image005.jpg>

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THIS IS EXHIBIT " B " TO
THE AFFIDAVIT OF
Allison Philpott
Sworn to before me
this 23 day of Oct , 2018
Ashley Tippett

**ASHLEY TIPPETT**
A Commissioner for Oaths in and for
the Province of Newfoundland and Labrador.
My commission expires on December 31, 2022.

## Philpott, Allison (St. John's)

**From:** Philpott, Allison (St. John's)
**Sent:** Tuesday, October 23, 2018 2:25 PM
**To:** Philpott, Allison (St. John's)
**Subject:** FW: Heddle Update

**From:** Macleod, Kurt (CA - Halifax) <kmacleod@deloitte.ca>
**Sent:** October 19, 2018 11:14 AM
**To:** PRINCE, Robert (MONCTON) <robert.prince@bdc.ca>
**Cc:** Jones, Neil X. (CA - Halifax) <neiljones@deloitte.ca>
**Subject:** Heddle Update

Bob,

Just wanted to provide you with an update. Shortly after I emailed you yesterday, we received an email from Dennis Thorne at Heddle Marine indicating that they would not be submitting a new offer to Management.

They did however indicate that the original $500 thousand offer was still available for consideration.

Regards,

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**Kurt MacLeod, MBA**
Manager | Financial Advisory Services
Deloitte
1969 Upper Water Street, Halifax, Nova Scotia, B3J 3R7, Canada
D: 1 (902) 721 5602 | M: 1 (902) 430 9930
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