Court File No: CV-20-00634195-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

BETWEEN:

ORIONIS CORPORATION

Applicant

- and -

ONTARIO GRAPHITE, LTD.

Respondent

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

BOOK OF AUTHORITIES OF THE APPLICANT
(Comeback Hearing; Returnable Feb. 20, 2020)

February 19, 2020

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COURT FILE NO.: CV-18-603054-00CL
DATE: 20181121

SUPERIOR COURT OF JUSTICE – ONTARIO
(COMMERCIAL LIST)

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

RE: IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF ARALEZ PHARMACEUTICALS INC. AND ARALEZ PHARMACEUTICALS CANADA INC., Applicants

BEFORE: S.F. Dunphy J.

COUNSEL: *Maria Konyukhova and Kathryn Esaw* for Applicants

Jeffrey Levine, for the Official Committee of Unsecured Creditors

David Bish, for Richter Advisory Group, Monitor

Danish Afroz, for Deerfield Management Company, L.P.

HEARD at Toronto: November 16, 2018

REASONS FOR DECISION

[1] This case raises for determination the always-troubling question of Key Employee Retention Plans (or "KERPs") and Key Employee Incentive Plans (or "KEIPs"). At the conclusion of the hearing. I indicated that I would be approving the proposed KERP involving three employees with reasons to follow and would take under reserve the matter of the proposed KEIP.

[2] For the reasons that follow, I have determined to approve the KEIP as well. My reasons that follow apply to both programs.

Background facts

[3] The applicants Aralez Pharmaceuticals Inc. and Aralez Pharmaceuticals Canada Inc. brought this application under the *Companies' Creditors Arrangement Act*, R.S.C. 1990, c. C.-36 and an initial order was granted by me on August 10, 2018 with Richter Advisory Group Inc. appointed as Monitor. A number of affiliated entities in the

same corporate group sought relief pursuant to Chapter 11 of the United States Bankruptcy Code on the same day. The Chapter 11 case is being managed by Justice Glenn in the United States Bankruptcy Court for the Southern District of New York. Both courts have adopted a cross-border protocol.

[4] As their names suggest, the Aralez group of companies are in the pharmaceutical industry. The debtor companies have operated in an integrated manner and have 41 employees at the Canadian entities and 23 in the Chapter 11 entities.

[5] In addition to being operationally integrated, Aralez has an integrated capital structure as well. The secured credit facility is secured by substantially all of the assets of the debtor companies on both sides of the border. The secured creditors – Deerfield Partners L.P. and Deerfield Private Design Fund III, L.P. – possess security on substantially all of the assets of the debtor companies on both sides of the border. The security in Canada has been subjected to independent review by the Monitor and its counsel and no issues have arisen nor have any creditors objected to their claims.

[6] These cases have been targeting a managed liquidation from the start. On September 18, 2018, the Canadian and US entities entered into three stalking horse agreements and, pursuant to a court-ordered sales process order, are in the process of completing a bid process in the coming days. The three stalking horse bids place a "floor" under sale proceeds of approximately $240 million subject to possible adjustments. This compares to the secured claim of Deerfield that is approximately $275 million.

[7] I understand that a motion may be brought in the United States to challenge some aspects of Deerfield's security in that jurisdiction (no such motion has been suggested in Canada to date). However, as things currently stand, the bid process underway would have to yield a fairly significant improvement from the existing stalking horse offers in order to result in surplus being available for junior creditor groups. The point of this analysis is merely to establish that Deerfield's input into the process of design of the KEIP and KERP programs before me is a material factor. Any funds diverted to KEIP or KERP programs have a substantial likelihood of coming out of Deerfield's pocket in the final analysis and any improvements or de-risking to either cash flow or sales proceeds will enure very substantially to Deerfield's benefit.

[8] Stated differently – Deerfield has significant "skin in the game" when it comes to a KERP or KEIP.

[9] Deerfield's interest acquires somewhat greater weight when one considers that one of the stalking horse bids (in the United States) is a credit bid whereas the Canadian stalking horse bid involves a sale of the assets of Aralez Pharmaceuticals Inc., resulting in the unsecured creditors of subsidiary Aralez Pharmaceuticals Canada Inc. being granted effective priority over Deerfield despite Deerfield's secured claims.

Deerfield is thus very likely to be one of the only Canadian creditors substantially impacted by the KEIP or KERP.

[10] This does not imply that the Court is a rubber stamp as to whatever Deerfield may have approved nor does it imply that other voices have no weight. It does imply that some comfort can be taken that this process has been subject to arm's length market discipline. Deerfield has an interest in getting as much as possible in the way of value-added effort out of the employee group and they have an interest in getting that effort at as low a cost as they can bargain for.

[11] The KERP program involved only three employees, was reported upon extensively by the Monitor and was not opposed by any stakeholder. I approved it at the hearing with reasons to follow (these are those reasons). The KEIP program affects nine senior management employees whose services are provided to both the Canadian and United States debtors and was accordingly presented to both courts for approval. I am advised that Justice Glenn approved the KEIP program for purposes of the United States debtors on November 19, 2018.

[12] While the KERP and KEIP programs were presented to me separately, they have many features in common. Were this not a transnational proceeding, it is quite likely that I should have had but a single combined KERP-KEIP program before me since these are not commonly differentiated in this jurisdiction. Different considerations obtain in the United States where KERP programs for some categories of employees are not allowed and KEIP programs are subject to specific rules one of which is that the predominant purpose of a KEIP must be *incentive* and not *retention*. Both are appropriate criteria in our process. In approving the KEIP program for the United States debtors, Justice Glenn indicated that he was satisfied that the KEIP program was designed primarily to incent the beneficiaries of the program.

[13] The Canadian KERP impacts three employee of Aralez Pharmaceuticals Canada Inc. The KERP would provide these three with a retention bonuses of between 25% and 50% of salary. The total amount payable under the proposed program would be $256,710 and payment is to be made on the earlier of termination without cause, death or permanent disability and the closing of a sale of the Canadian assets.

[14] The KEIP impacts nine senior management employees of the Canadian debtors who provide services (in all but one case) that benefit both estates. None of the KEIP participants are expected to have on-going roles once the bankruptcy sales process is completed. The program is designed to incent participants to assist in achieving the highest possible cash flow during the bankruptcy process (thereby reducing the need to rely upon DIP financing) and to achieve the highest level of sales proceeds. Cash flow is measured relative to the DIP budget and nothing is payable until sales are completed.

[15] The affected individuals are members of the senior management team that can be expected to be in a position to achieve a positive impact upon both criteria (cash flow and sales proceeds), but their roles are such that the level and value of the contributions of each towards those targets are difficult to measure with precision. Total payouts under the “super-stretch” targets could rise to as much as $4,058,360. This figure may be compared to the stalking horse bids that establish a floor price of $240 million.

[16] Since all but one of the participants in the KEIP program are providing services for the benefit of both United States and Canadian debtors, the KEIP program has been designed such that costs will be shared by the two estates regardless of residence.

[17] The design of the two programs was supervised by Alvarez & Marsal Inc, the financial advisor to the United States and Canadian debtors. The Compensation Committee of the parent company’s Board was involved as was the debtor’s counsel. The Monitor was consulted at every step in the process and provided significant input that was taken into account. The Board of Directors of each affected entity has approved the plans.

[18] The programs were disclosed to the proposed beneficiaries at or near the outset of the bankruptcy process. At the request of the DIP Lender, court approval of these programs was not sought at that time as is relatively common. The stalking horse bids were several weeks away from being finalized and significant effort from the affected employees would be needed to but those transactions to bed. The sales process that followed also needed to be put on the rails and the all hands were needed to ensure that the business passed through the initial stages of the bankruptcy filing without undue adversity. In short, the affected employees were asked to acquiesce in the deferral of approval of these programs with the understanding that the employer would pursue their approval in good faith.

[19] With only a few weeks remaining until the expected end of the sales process, it is fair to observe the employees have more than delivered on their end of the bargain. Cash flow has held up very well and the stalking horse bids have been firmed up at a favourable level.

[20] The motion for approval of the KEIP (not the KERP) was opposed by the Official Committee of the Unsecured Creditors appointed pursuant to the United States Chapter 11 process. I shall not review here the nature of their standing claim – and the dispute of that claim. Their intervention has been focused, their arguments precise and the prospect of harm in the form of unnecessary delay or expense is minimal. Without prejudice to the position of everyone on the status of this committee in other contexts, I agreed to hear them and receive their written arguments. The cross-border protocol that both courts have approved affords me discretion to allow the Official Committee standing on a case-specific or *ad hoc* basis.

[21] In the view of the Official Committee, the KEIP program bonuses are too high and too easily earned. I shall address both of these arguments below.

Issues to be determined

[22] Ought this court to exercise its discretion to approve the KERP or KEIP programs as proposed by the applicants?

Analysis and discussion

[23] KERP/KEIP programs throw up a number of thorny issues that must be grappled with because there are a number of potentially conflicting policy considerations to balance.

[24] The early stages of an insolvency filing are chaotic enough without having added pressures of trying stem the hemorrhage of key employees. “Key” is of course an elastic concept. Everyone is key to someone. Employees are not hired to amuse management but to perform necessary functions. Sorting out “key” in the context of the organized chaos that is the early days of an insolvency filing requires a weathered eye to be cast in multiple directions at once:

- restructuring businesses often have inefficiencies that need identifying and resolving that may impact some otherwise “key” employees;

- with the levers of traditional shareholder oversight blunted in insolvency, the risks of management resolving conflicts in favour of self-interest are acute;

- it is easy to overstate the risk of loss of key employees if a “bunker mentality” causes management to take counsel of their fears rather than objective evidence, such evidence to be informed by a recognition that *some* degree of instability is inevitable; and

- “business as usual” is a goal, but never a perfectly achievable one and small amounts of stability acquired at high cost may be a bad investment.

[25] While the risks of abuse or wasted effort are easily conjured, the legitimate use of an appropriately-calibrated incentive plan are equally obvious:

- Employees in newly-insecure positions are easy prey to competitors able to offer the prospect of more stable employment, sometimes even at lower salary levels, to people whose natural first priority is looking after their families;

- There is a risk that the most employable and valuable employees will be cherry-picked while the debtor company may find itself substantially handicapped in trying to compete for replacement employees;

- Whether by reason of internal restructuring or a court-supervised sales process, employees may often find themselves being asked to bring all of their skills and devotion to the task of putting themselves out of work; and

- Since many employers use a mix of base salary and profit-based incentives, employees of an insolvent business in restructuring may find themselves being asked to do more – sometimes covering for colleagues who have being laid off or who have left for greener pastures - while earning a fraction of their former income.

[26] What is wanting to sort out these competing interests is one thing that the court – on its own at least – is singularly ill-equipped to provide. It is here that the essential role of the Monitor as the proverbial “eyes and ears of the court” comes to the fore. The court cannot shed its robe and wade into the debate in a substantive way. The Monitor on the other hand can shape the manner in which the debate is conducted and in which the decisions presented to the court for approval are made.

[27] What the court is unable to supply on its own can be summed up in the phrase “business judgment”. Outside of bankruptcy, the debtor company is entitled to exercise its own business judgment in designing such programs subject to the oversight of shareholders and the directors they appoint. Inside bankruptcy, the oversight of the court is required to assess the reasonableness of the exercise of the debtor company’s business judgment. In my view, the court’s role in assessing a request to approve a KERP or KEIP program is to assess the totality of circumstances to determine whether the process has provided a reasonable means for *objective* business judgment to be brought to bear and whether the end result is objectively reasonable.

[28] Perfect objectivity, like the Holy Grail, is unattainable. However, where business judgment is applied in a process that has taken appropriate account of as many of the opposing interests as can reasonably be brought into the equation, the result will adhere most closely to that unattainable ideal.

[29] My review of the limited case law on the subject of KERP (or KEIP) approvals suggests that there are no hard and fast rules that can be applied in undertaking this task. However the principles to be applied do emerge. Morawetz J. suggested a number of considerations in *Cinram International Inc. (Re),* 2012 ONSC 3767 (CanLII),

relying on the earlier decision of Newbould J. in *Grant Forest Products Inc. (Re)*, 2009 CanLII 42046 (ON SC)[1]. I reproduce here the synthesis of Morawetz J. (*Cinram*, para. 91):

a. whether the Monitor supports the KERP agreement and charge (to which great weight was attributed);
b. whether the employees to which the KERP applies would consider other employment options if the KERP agreement were not secured by the KERP charge;
c. whether the continued employment of the employees to which the KERP applies is important for the stability of the business and to enhance the effectiveness of the marketing process;
d. the employees' history with and knowledge of the debtor;
e. the difficulty in finding a replacement to fulfill the responsibilities of the employees to which the KERP applies;
f. whether the KERP agreement and charge were approved by the board of directors, including the independent directors, as the business judgment of the board should not be ignored;
g. whether the KERP agreement and charge are supported or consented to by secured creditors of the debtor; and
h. whether the payments under the KERP are payable upon the completion of the restructuring process.

[30] I have conducted my examination of the facts of this case having regard to the following three criteria which I think sweep in all of the considerations underlying *Grant* and *Cinram* and which provide a framework to consider the degree to which appropriately objective business judgment underlies the proposal:

(a) Arm's length safeguards: The court can justifiably repose significant confidence in the objectivity of the business judgment of parties with a legitimate interest in the matter who are independent of or at arm's length from the beneficiaries of the program. The greater the arm's length input to the design, scope and implementation, the better. Given the obvious conflicts management find themselves in, it is important that the Monitor be actively involved in all phases of the process – from assessing the need and scope to designing the targets and metrics and the rewards. Creditors who may fairly be considered to be the ones indirectly

[1] See also Pepall J. (as she then was) in *Canwest Global Communications Corp. (Re)*, 2009 CanLII 55114 (ON SC) at para. 49-52.

benefitting from the proposed program and indirectly paying for it also provide valuable arm's length vetting input.

(b) Necessity: Incentive programs, be they in the form of KERP or KEIP or some variant are by no means an automatic or matter of course evolution in an insolvency file. They need to be justified on a case-by-case basis on the basis of necessity. Necessity itself must be examined critically. Employees working to help protect their own long-term job security are already well-aligned with creditor interests and might generally be considered as being near one end of the necessity spectrum while those upon whom great responsibility lies but with little realistic chance of having an on-going role in the business are the least aligned with stakeholder interests and thus may generally be viewed as being near the other end of the necessity spectrum when it comes to incentive programs. Employees in a sector that is in demand pose a greater retention risk while employees with relatively easily replaced skills in a well-supplied market pose a lesser degree of risk and thus necessity. Overbroad programs are prone to the criticism of overreaching.

(c) Reasonableness of Design: Incentive programs are meant to align the interests of the beneficiaries with those of the stakeholders and not to reward counter-productive behavior nor provide an incentive to insiders to disrupt the process at the least opportune moment. The targets and incentives created must be reasonably related to the goals pursued and those goals must be of demonstrable benefit to the objects of the restructuring process. Payments made before the desired results are achieved are generally less defensible.

(a) Arm's length safeguards

[31] In my view, there is substantial evidence that the process of negotiating and designing both programs has benefitted from significant arm's length and objective oversight in the negotiation, design and implementation phases of these two programs.

[32] The process leading to both programs began prior to the insolvency filings on August 10, 2018. Aralez had engaged A&M as its financial advisor for the restructuring process and asked A&M to help formulate both the key employee incentive and retention programs. A&M worked on program design in consultation with the debtor's legal counsel and with input from the compensation committee of the Aralez Pharmaceuticals Inc. Board of Directors, none of whom are beneficiaries of either program.

[33] The Monitor has been consulted extensively. The Monitor has inquired into the design and objects of the proposed plans and has verified the levels of the proposed

incentives relative to the objectives of the programs and other historical data. The Monitor's input has resulted in a number of alterations to the proposals as these have evolved. As the programs have emerged from the process, the Monitor's conclusion is that the KERP is comparable to other KERP plans this court has approved and is reasonable in the circumstances. The Monitor has concluded that the KEIP addresses the concerns raised by the Monitor, protects the interest of Canadian stakeholders and these would not be materially prejudiced by approval of the KEIP. Both recommendations are entitled to very significant weight from this court.

[34] The U.S. Trustee raised a number of concerns with the proposed KEIP which have also resulted in revisions.

[35] Finally, Deerfield has been consulted and has indicated that they take no objection to either program as they have emerged from this process. For the reasons discussed above, Deerfield's *imprimatur* carries a particularly significant degree of weight in these circumstances in terms of establishing the arm's length and market-tested nature of the two programs before me.

[36] The business judgment of Deerfield and the Board of Directors of API are entitled to significant weight. The independent and very significant input of the Monitor, A&M and the U.S. Trustee afford significant comfort that objective viewpoints have played a significant role in designing and vetting the proposals. Finally, the recommendation of the Monitor is entitled to significant weight given the unique role the Monitor plays in the Canadian restructuring process.

[37] In summary, the process followed provides a high degree of comfort that a reasonable level of objective business judgment has been brought to bear. Circumstances will not allow every case the luxury of such a thorough process. However, this process was professionally designed thoroughly run. It has appropriately generated a high level of confidence in the integrity of the outcome

(b) Necessity

[38] The design of the two programs demonstrates an appropriate regard for the criterion of necessity. They are not over-broad.

[39] Any analysis of whether a program is over-broad must take into account the nature of the business. In some respects, Aralez may be likened to a virtual pharmaceutical company in that it out-sources many functions of a traditional pharmaceutical company such as manufacturing. It thus has relatively few employees compared to its size.

[40] In designing the programs and assessing which employees to be included, an assessment was undertaken of each prospective beneficiary in terms of the ease with which they might be replaced, the degree to which they are critical to daily operations of

the debtor companies or completion of the sales process and – for the KERP program at least – the perceived level of retention risk. The Monitor's input was sought at each level of the design and finalization of the programs.

[41] The KERP program involves three employees in Canada and I am advised that their inclusion in the KERP is a condition of the purchaser under the stalking-horse bid. The loss of these three employees – critical to the Canadian business being sold – would endanger the stalking horse bid process at worst and disrupt the business being sold by requiring the debtor companies to deal with recruiting, transition and similar matters at a juncture where they are least able to deal with them at best. Their departure at this juncture would entail significant additional expenditures in terms of professional time at least if that event did not endanger the stalking horse bid.

[42] The KEIP program involves nine members of senior management. They are employees the nature of whose function defies precise description or measurement. They are employees who act in concert with each other as part of a team for whom neither the clock nor the calendar play more than a subsidiary role in dictating their hours of labour. These employees are essential to ensuring the business remains stable and performs well during the restructuring process. They play a key role in helping ensure the sales process achieves the highest level of return. They are also employees most of whom are laboring under the near certainty that the more efficient and successful they are in their efforts, the sooner they will be out of a job.

[43] At such a high level, personal reputation and professional pride remain as significant motivators to be sure. While a job well done may be its own reward, appropriate financial incentives are not without their place. This is a classic case for a well-designed incentive program.

[44] I am satisfied that the design of these programs satisfies the criterion of necessity.

(c) Reasonableness of design

[45] The KERP program provides for retention bonuses ranging from 25% to 50% of annual salary. The aggregate compensation available is $256,710, a figure that may be contrasted to the stalking horse bid for the Canadian assets of $62.5 million. Payment is made on the earlier of termination without cause by the company, death or permanent disability and the completion of the sales transaction.

[46] The timing of payments and the amount of the payments provided for, relative both to the salary of the individuals and to the value of the company, are both well in-line with precedent.

[47] The KEIP program provides for incentive payments to participants based on the debtors' performance relative to target established for cash flow targets during the

bankruptcy proceedings and relative to the achieved asset sale proceeds. Failure to reach targets results in no bonus, while four levels of bonus are possible (Threshold[2], Target, Stretch and Super Stretch).

[48] The real controversy on the motion was in respect of the KEIP.

[49] It is true that the cash flow performance of the debtors to date plus the projections of cash flow over the coming weeks put the KEIP participants well on track to achieving the highest "super-stretch" level of incentive. It is also true that if *no* bids are received in the sales process now underway and only the stalking horse bids are completed, the participants will be comfortably within the "target" level of incentive for asset sales. Combined, this means that that total incentives of approximately 81.25% of salary appears to be all but assured to KEIP participants. In the circumstances, the Official Committee objects that these incentives are simply too easily earned.

[50] They also object to the level of incentives relative to salary as being unacceptably high.

[51] The answer to both of these objections lies in the peculiar facts of this case.

[52] The KERP and KEIP programs were both conceived of and designed primarily in the period leading up to the initial filings made in August 2018, although alterations have been made following the input of, among others, the United States trustee. The employees selected for inclusion in both programs have been operating in the expectation that the employer would proceed in good faith to seek court approval as soon as practicable. At the request of the DIP Lender, the process of seeking court approval was deferred to put priority on the process of securing and finalizing the stalking horse bids and getting the sales process underway. At the time these plans were first offered to employees, forecasting cash flow in bankruptcy and sales proceeds was looking through a glass darkly. It is only hindsight – and the past efforts of the employees – that has made the targets appear to be such an easy goal.

[53] Of course, the employer could not promise and the employee could not expect that court approval of these plans would be a rubber stamp. That does not mean that this court should not take into account the circumstances prevailing when the plans were first offered to employees and the good faith of the employees in continuing to apply their shoulders to the wheel without causing disruption to the process when it could least afford it. It would be fundamentally unfair to penalize the affected employees for their good faith and constructive behavior in this case. It would also be counter-productive as such a precedent would not fail to alter behavior in future cases.

---

[2] The threshold incentive based on cash flow was removed after discussions with the United States Trustee.

[54] I am satisfied that the targets were realistic and appropriate at the time they were set and served to align the interests of employees with stakeholders in an appropriate manner.

[55] The level of incentive is also less than meets the eye when the facts are examined more closely. While the combined cash flow plus asset sale incentives could result in incentives of up to 125% of salary, that figure is premised on base salary. In the case of the employees within the proposed KEIP program, base salary has been but one portion of their total compensation. When historical compensation is taken into account, the incentive payments recede to levels significantly below the 80% level calculated by the Official Committee to something closer to 50%.

[56] I am satisfied that the incentive amounts are reasonable in all of the circumstances.

Disposition

[57] In the result, I confirmed the KERP program at the hearing of the motion on December 16, 2018 and am granting the motion in respect of the KEIP program at this time. My approval extends to the requested priority charges securing the KEIP payments.

[58] Order accordingly.

_____

S.F. Dunphy J.

Date: November 21, 2018

Tab 2

2009 CarswellOnt 7627
Ontario Superior Court of Justice [Commercial List]

Brainhunter Inc., Re

2009 CarswellOnt 7627, [2009] O.J. No. 5207, 183 A.C.W.S. (3d) 28

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

AND IN THE MATTER of a Plan of Compromise or Arrangement of Brainhunter Inc., TrekLogic Inc., Brainhunter Canada Inc., Brainhunter (Ottawa) Inc. and Protec Employment Services Limited (Applicants)

APPLICATION UNDER SECTION 18.6 OF THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS AMENDED

Newbould J.

Heard: December 2, 2009
Judgment: December 4, 2009
Docket: 09-8483-00CL

Counsel: Jay A. Swartz, James D. Bunting for Applicants
Grant B. Moffat for Deloitte and Touche Inc.
Edmond Lamek for Toronto-Dominion Bank
Joseph Bellissimo for Roynat Capital Inc.
Daniel R. Dowdall for certain noteholders
Patrick F. Schindler for an unsecured judgment creditor

Subject: Insolvency

Headnote

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Arrangements — Approval by court — Discretion of court

Canadian Company, located in Toronto, provided human resources services to clients — Bank was secured creditor of Company and agreed to provide applicants with $7 million to meet working capital requirements during Companies' Creditors Arrangement Act (CCAA) proceedings — Company made application for protection under s. 18.6 of CCAA — Company intended to solicit going concern asset sale of business, which meant no plan of arrangement filed — Application allowed — Court can allow CCAA protection in cases where company does not file formal plan of compromise or arrangement.

Table of Authorities

Cases considered by *Newbould J.*:

Canwest Global Communications Corp., Re (2009), 2009 CarswellOnt 7169 (Ont. S.C.J. [Commercial List]) — considered

Consumers Packaging Inc., Re (2001), 150 O.A.C. 384, 27 C.B.R. (4th) 197, 2001 CarswellOnt 3482, 12 C.P.C. (5th) 208 (Ont. C.A.) — followed

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

Statutes considered:

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

s. 3 — referred to

s. 9 — referred to

s. 11.2(1) [en. 2005, c. 47, s. 128] — considered

s. 11.4 [en. 2005, c. 47, s. 128] — considered

s. 11.4(1) [en. 1997, c. 12, s. 124] — considered

s. 11.4(2) [en. 1997, c. 12, s. 124] — considered

s. 11.4(3) [en. 1997, c. 12, s. 124] — considered

s. 11.4(4) [en. 1997, c. 12, s. 124] — considered

s. 11.51(1) [en. 2005, c. 47, s. 128] — considered

s. 11.52(1) [en. 2007, c. 36, s. 66] — considered

s. 36(1) — considered

APPLICATION by company for protection under s. 18.6 of *Companies' Creditors Arrangement Act*.

***Newbould J.*:**

1 On December 2, 2009 after hearing submissions from the parties present, I made an initial order granting CCAA protection to the applicants, with reasons to follow. These are my reasons.

2 There is no question that the Court has jurisdiction to hear the application pursuant to section 9 of the CCAA as the applicants' head offices are located in Toronto, Canada. At the time of the application, Brainhunter Inc. was listed on the TSX. The applicants qualify as debtor companies pursuant to section 3 of the CCAA as the applicants are affiliated companies with total claims against them of more than $5 million. The applicants are all insolvent.

3 The applicants are in the business of providing human resources with the skill sets to satisfy their clients' needs. The applicants' business operates in large part through umbrella agreements generally referred to as Master Service Agreements. These agreements are entered into by the applicable applicant and each of their respective contract staffing clients.

4 Each time a contract staffing client wishes to retain the services of an individual (each a "Contractor") pursuant to a Master Services Agreement, the client will enter into a sub-agreement referred to as a statement of work in respect of the specific Contractor. The applicable applicant subsequently enters into an agreement with the Contractor to fulfill the statement of work and the Contractor issues invoices to the applicant for the work he or she performs for the client. The applicant then pays the Contractor and bills the client. Because the applicants receive payment from their clients after they pay their Contractors, the

applicants are dependent on having adequate credit facilities available to fund the payments to Contractors until the related invoices from the client can be collected.

5 TD Bank and Roynat are secured creditors with security over all of the assets of the applicants. As at October 31, 2009 there was principal outstanding of $18.7 million to TD Bank and principal and interest of $5.9 million owing to Roynat.

6 In addition there are secured subordinated promissory notes secured only on the assets of Brainhunter Inc. The principal and interest outstanding as at October 31, 2009 was $11.9 million. Most of the material assets of the applicants are not held in Brainhunter Inc., but by the other applicants.

7 TD Bank and the applicants have entered into a debtor-in-possession financing term sheet, pursuant to which the TD Bank has agreed to provide the applicants with $7 million of DIP financing to enable the applicants to meet their working capital requirements during the CCAA proceedings.

8 This application is in some respects unusual because the applicants state that they intend at the outset to solicit a going concern asset sale of the business, and that it is likely that there will be no plan of arrangement filed. The factum on their behalf states:

> 5. If protection is granted under the CCAA, the Applicants intend to bring a motion seeking approval of a bid process to solicit going concern asset purchase offers for the Applicants' business, as well as offers to sponsor a plan of arrangement (the "Bid Process"). The Applicants have entered into an agreement to sell substantially all of their assets as a going concern on the understanding that this agreement will serve as a stalking horse bid. The Bid Process will solicit competing offers from prospective investors to bid up the stalking horse bid.
>
> 24. Although the proposed Bid Process could result in the filing of a plan of arrangement or plan of compromise, it is more likely to result in the sale of the Applicants' business.

9 The applicants submit that this Court has the jurisdiction to provide them with protection under the CCAA in circumstances such as these where the applicants may not file a formal plan of compromise or arrangement.

10 I agree with the applicants that protection under the CCAA may be granted in these circumstances. I say that for the following reasons.

11 The initial protection is supported by TD Bank and Roynat. It is also supported by the secured noteholders represented by Mr. Dowdall, being a little more than 60% of the noteholders. Mr. Dowdall has other concerns that I will deal with.

12 It is well settled in Ontario that a court in a CCAA proceeding may approve a sale of all or substantially all of the assets of a debtor company as a going concern. In *Consumers Packaging Inc., Re*, 27 C.B.R. (4th) 197 (Ont. C.A.), the Court stated:

> The sale of Consumers' Canadian glass operations as a going concern pursuant to the Owens-Illinois bid allows the preservation of Consumers' business (albeit under new ownership), and is therefore consistent with the purposes of the CCAA.

13 Similarily, it is well settled in Ontario that a court in a CCAA proceeding may order the sale of a business in the absence of a plan of arrangement being put to stakeholders for a vote. In *Nortel Networks Corp., Re* (2009), 55 C.B.R. (5th) 229 (Ont. S.C.J. [Commercial List]) Morawetz J. came to this conclusion after analyzing a number of cases that had made such an order. See paras 35 to 40 of his reasons for judgment.

14 It seems to me that if at some point in time after an initial CCAA protection order has been made, it appears appropriate to undertake a sales process to sell the business without a plan of arrangement in place, there is no reason why CCAA protection should not initially be granted if at the outset it is thought appropriate to undertake a sales process without a plan of arrangement in place. It is simply a matter of timing as to when it appears appropriate to pursue a sale of the business without a plan of arrangement in place.

15 *Nortel Networks Corp., Re* was decided before the new CCAA provisions came into force on September 18, 2009. The new relevant provision does not, however, affect the principles accepted by Morawetz J. in that case. Section. 36(1) provides:

> 36.(1) A debtor company in respect of which an order has been made under this Act may not sell or otherwise dispose of assets outside the ordinary course of business unless authorized to do so by a court. Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained.

16 In *Canwest Global Communications Corp., Re* [2009 CarswellOnt 7169 (Ont. S.C.J. [Commercial List])] released November 12, 2009, Pepall J. stated the following regarding s. 36:

> The CCAA is remedial legislation designed to enable insolvent companies to restructure. As mentioned by me before in this case, the amendments do not detract from this objective. In discussing section 36, the Industry Canada Briefing Book on the amendments states that "The reform is intended to provide the debtor company with greater flexibility in dealing with its property while limiting the possibility of abuse."

17 The applicants have not yet brought their motion for approval of a sales process, and consideration as to whether such a sales process is appropriate will take place when the motion is heard. [1] The fact that the motion was anticipated at the time of the initial order with no plan of arrangement in sight does not mean however that the initial order should not be made.

18 The applicants seek an order declaring that the Contractors are "critical suppliers", permitting the payment of pre-filing amounts to the contractors and creating a charge that secures the obligations owed to the Contractors.

19 The authorization to pay pre-filing amounts is now codified in section 11.4 of the CCAA. Pursuant to this section, the Court has the discretion to:

> (a) declare a person to be a critical supplier, if it is satisfied the person is a supplier of goods or services to the company and the goods or services are critical to the company's continued operations (s. 11.4(1));
>
> (b) make an order requiring the "critical supplier" to supply any goods or services specified by the Court to the company on any terms and conditions that are consistent with the supply relationship or the Court considers appropriate (s. 11.4(2));
>
> (c) grant a charge in favour of a person declared to be a critical supplier, in an amount equal to the value of the goods or services supplied under the terms of the order (s. 11.4(3)); and
>
> (d) order the security or charge to rank in priority over the claim of any secured creditor of the company (s. 11.4(4)).

20 The rationale for the enactment of section 11.4 is explained in the Industry Canada Clause by Clause Briefing Book as follows:

> Companies undergoing a restructuring must be able to continue to operate during the period. On the other hand, suppliers will attempt to restrict their exposure to credit risk by denying credit or refusing services to those debtor companies. To balance the conflicting interests, the court will be given the authority to designate certain key suppliers as "critical suppliers". The designation will mean that the supplier will be required to continue its business relationship with the debtor company but, in return, the critical supplier will be given security for payment.

21 The applicants submit, and I accept, that an order permitting the payment of pre-filing amounts is necessary to ensure the continued provision of personal services from the Contractors to the applicants and to prevent the potentially significant harm that could follow if such payments are not made. If the Contractors are not paid for services provided before the filing of the application, there is a substantial risk they will not continue to perform services under the current statements of work. This would result in a default by the applicants to their clients and impact the ability of the applicants to continue as a going concern.

22 As the Contractors are individuals, the applicants did not seek an order requiring the continued supply of personal services. However, they requested a charge to secure payment to the Contractors in order to provide assurances to the Contractors that their relationship will be unaffected during the CCAA proceedings. The amount of the Contractors' charge requested is $15 million which represents an estimated average of the amount owing to Contractors. The applicants requested that the Contractors' charge rank in priority to all secured lenders other than the TD Bank. Roynat is agreeable to that and the notesholders represented here do not oppose it. Deloitte & Touche Inc, in their capacity as the proposed monitor, in their pre-filing report support the charge as reasonable.

23 I am satisfied that it is appropriate to provide in the initial order that the Contractors are declared to be critical suppliers, that the applicants shall be entitled to pay outstanding and future amounts owing to Contractors and that a Contractors' charge as requested be provided.

24 The applicants also requested other charges, being (i) an administration charge of $1 million: (ii) a KERP charge of $290,000 under which the CEO is to be paid a retention bonus of $50,000 for two months in addition to his salary and 10 key employees will be paid up to $190,000 if they remain with the company for four months from the date of filing: (iii) a directors and officers charge of $1.7 million; and (iv) a DIP charge to secure the $7 million DIP facility being provided by TD Bank.

25 TD Bank and Roynat support these charges and their priority provided for in the initial order. Deloitte & Touche Inc. expressed the view that the proposed charges are necessary and reasonable and will provide the applicants with the opportunity to successfully complete a restructuring.

26 Mr. Dowdall for the noteholders raised a concern with some of these charges. He said that while counsel for the applicants discussed with him in advance the intention to file, he was not made aware of the details and his clients have not had an opportunity to review the information provided in the material filed with the Court. Thus he wishes to reserve his clients' rights with respect to these charges. He has a concern that while typically such concerns when raised at the initial application are met with the response that there is a come-back clause in the initial order, people start relying on the charges and it becomes difficult to oppose them as time passes. I think his concern is a fair one. In this case, however, not only is there a come-back clause with a 7 days notice requirement, but the matter will be before the Court shortly on December 8, 2009 when the motion to approve a sales process will be dealt with. Mr. Dowdall's clients will have had an opportunity to consider their position before then and be able to move to vary the initial order if they so desire.

27 In the circumstances, on the basis of the record before me, the charges appear appropriate and are approved. This is without prejudice, however, to the noteholders right to contest them. Any delay, however, in taking steps to contest them will obviously seriously affect any attack on them.

28 Mr. Schindler represents an unsecured judgment creditor owed approximately $250,000. His client of course had not seen the material before it was filed, and Mr. Schindler said that he had been intending to ask that the entire matter be adjourned for a week, and that he was asking that the charges not be made for at least a week to provide his client with time to consider whether they are warranted.

29 In exercising the balancing of interests required in a CCAA application, it would be risky indeed to delay the application or these charges at the request of one unsecured creditor. These are standard charges and deemed necessary by the proposed monitor. It should be noted that the sections of the CCAA under which the charges are authorized, being sections 11.2(1), 11.4(1), 11.51(1) and 11.52(1), provide that notice of a request for such charges is to be given to the secured creditors who are likely to be affected by the charge. Notice is not required to be given to unsecured creditors. In the circumstances, I declined the request to delay the charges.

Application allowed.

Footnotes

1 The motion is now scheduled for December 8, 2009

End of Document

Tab 3

COURT FILE NO.: CV-09-8241-OOCL
DATE: 20091112

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

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

AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT OF CANWEST GLOBAL COMMUNICATIONS CORP. AND THE OTHER APPLICANTS LISTED ON SCHEDULE "A"

BEFORE: PEPALL J.

COUNSEL: *Lyndon Barnes and Jeremy Dacks* for the Applicants
Alan Merskey for the Special Committee of the Board of Directors of Canwest
David Byers and Maria Konyukhova for the Monitor, FTI Consulting Canada Inc.
Benjamin Zarnett for the Ad Hoc Committee of Noteholders
Peter J. Osborne for Proposed Management Directors of National Post
Andrew Kent and Hilary Clarke for Bank of Nova Scotia, Agent for Senior Secured Lenders to LP Entities
Steve Weisz for CIT Business Credit Canada Inc.
Amanda Darroch for Communication Workers of America
Alena Thouin for Superintendent of Financial Services

REASONS FOR DECISION

Relief Requested

[1] The CMI Entities move for an order approving the Transition and Reorganization Agreement by and among Canwest Global Communications Corporation ("Canwest Global"), Canwest Limited Partnership/Canwest Societe en Commandite (the "Limited Partnership"), Canwest Media Inc. ("CMI"), Canwest Publishing Inc./Publications Canwest Inc ("CPI"), Canwest Television Limited Partnership ("CTLP") and The National Post Company/ La Publication National Post (the "National Post Company") dated as of October 26, 2009, and which includes the New Shared Services Agreement and the National Post Transition Agreement.

[2] In addition they ask for a vesting order with respect to certain assets of the National Post Company and a stay extension order.

[3] At the conclusion of oral argument, I granted the order requested with reasons to follow.

Backround Facts

(a) Parties

[4] The CMI Entities including Canwest Global, CMI, CTLP, the National Post Company, and certain subsidiaries were granted *Companies' Creditors Arrangement Act ("CCAA")* protection on Oct 6, 2009. Certain others including the Limited Partnership and CPI did not seek such protection. The term Canwest will be used to refer to the entire enterprise.

[5] The National Post Company is a general partnership with units held by CMI and National Post Holdings Ltd. (a wholly owned subsidiary of CMI). The National Post Company carries on business publishing the National Post newspaper and operating related on line publications.

(b) History

[6] To provide some context, it is helpful to briefly review the history of Canwest. In general terms, the Canwest enterprise has two business lines: newspaper and digital media on the one hand and television on the other. Prior to 2005, all of the businesses that were wholly owned by Canwest Global were operated directly or indirectly by CMI using its former name, Canwest Mediaworks Inc. As one unified business, support services were shared. This included such things as executive services, information technology, human resources and accounting and finance.

[7] In October, 2005, as part of a planned income trust spin-off, the Limited Partnership was formed to acquire Canwest Global's newspaper publishing and digital media entities as well as certain of the shared services operations. The National Post Company was excluded from this acquisition due to its lack of profitability and unsuitability for inclusion in an income trust. The Limited Partnership entered into a credit agreement with a syndicate of lenders and the Bank of

Nova Scotia as administrative agent. The facility was guaranteed by the Limited Partner's general partner, Canwest (Canada) Inc. ("CCI"), and its subsidiaries, CPI and Canwest Books Inc. (CBI") (collectively with the Limited Partnership, the "LP Entities"). The Limited Partnership and its subsidiaries then operated for a couple of years as an income trust.

[8] In spite of the income trust spin off, there was still a need for the different entities to continue to share services. CMI and the Limited Partnership entered into various agreements to govern the provision and cost allocation of certain services between them. The following features characterized these arrangements:

- the service provider, be it CMI or the Limited Partnership, would be entitled to reimbursement for all costs and expenses incurred in the provision of services;

- shared expenses would be allocated on a commercially reasonable basis consistent with past practice; and

- neither the reimbursement of costs and expenses nor the payment of fees was intended to result in any material financial gain or loss to the service provider.

[9] The multitude of operations that were provided by the LP Entities for the benefit of the National Post Company rendered the latter dependent on both the shared services arrangements and on the operational synergies that developed between the National Post Company and the newspaper and digital operations of the LP Entities.

[10] In 2007, following the Federal Government's announcement on the future of income fund distributions, the Limited Partnership effected a going-private transaction of the income trust. Since July, 2007, the Limited Partnership has been a 100% wholly owned indirect subsidiary of Canwest Global. Although repatriated with the rest of the Canwest enterprise in 2007, the LP Entities have separate credit facilities from CMI and continue to participate in the shared services arrangements. In spite of this mutually beneficial interdependence between the LP Entities and the CMI Entities, given the history, there are misalignments of personnel and services.

(c) Restructuring

[11] Both the CMI Entities and the LP Entities are pursuing independent but coordinated restructuring and reorganization plans. The former have proceeded with their *CCAA* filing and prepackaged recapitalization transaction and the latter have entered into a forbearance agreement with certain of their senior lenders. Both the recapitalization transaction and the forbearance agreement contemplate a disentanglement and/or a realignment of the shared services arrangements. In addition, the term sheet relating to the CMI recapitalization transaction requires a transfer of the assets and business of the National Post Company to the Limited Partnership.

[12] The CMI Entities and the LP Entities have now entered into the Transition and Reorganization Agreement which addresses a restructuring of these inter-entity arrangements. By agreement, it is subject to court approval. The terms were negotiated amongst the CMI Entities, the LP Entities, their financial and legal advisors, their respective chief restructuring advisors, the Ad Hoc Committee of Noteholders, certain of the Limited Partnership's senior lenders and their respective financial and legal advisors.

[13] Schedule A to that agreement is the New Shared Services Agreement. It anticipates a cessation or renegotiation of the provision of certain services and the elimination of certain redundancies. It also addresses a realignment of certain employees who are misaligned and, subject to approval of the relevant regulator, a transfer of certain misaligned pension plan participants to pension plans that are sponsored by the appropriate party. The LP Entities, the CMI Chief Restructuring Advisor and the Monitor have consented to the entering into of the New Shared Services Agreement.

[14] Schedule B to the Transition and Reorganization Agreement is the National Post Transition Agreement.

[15] The National Post Company has not generated a profit since its inception in 1998 and continues to suffer operating losses. It is projected to suffer a net loss of $9.3 million in fiscal year ending August 31, 2009 and a net loss of $0.9 million in September, 2009. For the past seven years these losses have been funded by CMI and as a result, the National Post Company owes CMI approximately $139.1 million. The members of the Ad Hoc Committee of Noteholders had agreed to the continued funding by CMI of the National Post Company's short-term liquidity needs but advised that they were no longer prepared to do so after October 30, 2009. Absent funding, the National Post, a national newspaper, would shut down and employment would be lost for its 277 non-unionized employees. Three of its employees provide services to the LP Entities and ten of the LP Entities' employees provide services to the National Post Company. The National Post Company maintains a defined benefit pension plan registered under the Ontario Pension Benefits Act. It has a solvency deficiency as of December 31, 2006 of $1.5 million and a wind up deficiency of $1.6 million.

[16] The National Post Company is also a guarantor of certain of CMI's and Canwest Global's secured and unsecured indebtedness as follows:

Irish Holdco Secured Note- $187.3 million

CIT Secured Facility- $10.7 million

CMI Senior Unsecured Subordinated Notes- US$393.2 million

Irish Holdco Unsecured Note- $430.6 million

[17] Under the National Post Transition Agreement, the assets and business of the National Post Company will be transferred as a going concern to a new wholly-owned subsidiary of CPI (the "Transferee"). Assets excluded from the transfer include the benefit of all insurance policies, corporate charters, minute books and related materials, and amounts owing to the National Post Company by any of the CMI Entities.

[18] The Transferee will assume the following liabilities: accounts payable to the extent they have not been due for more than 90 days; accrued expenses to the extent they have not been due for more than 90 days; deferred revenue; and any amounts due to employees. The Transferee

will assume all liabilities and/or obligations (including any unfunded liability) under the National Post pension plan and benefit plans and the obligations of the National Post Company under contracts, licences and permits relating to the business of the National Post Company. Liabilities that are not expressly assumed are excluded from the transfer including the debt of approximately $139.1 million owed to CMI, all liabilities of the National Post Company in respect of borrowed money including any related party or third party debt (but not including approximately $1,148,365 owed to the LP Entities) and contingent liabilities relating to existing litigation claims.

[19] CPI will cause the Transferee to offer employment to all of the National Post Company's employees on terms and conditions substantially similar to those pursuant to which the employees are currently employed.

[20] The Transferee is to pay a portion of the price or cost in cash: (i) $2 million and 50% of the National Post Company's negative cash flow during the month of October, 2009 (to a maximum of $1 million), less (ii) a reduction equal to the amount, if any, by which the assumed liabilities estimate as defined in the National Post Transition Agreement exceeds $6.3 million.

[21] The CMI Entities were of the view that an agreement relating to the transfer of the National Post could only occur if it was associated with an agreement relating to shared services. In addition, the CMI Entities state that the transfer of the assets and business of the National Post Company to the Transferee is necessary for the survival of the National Post as a going concern. Furthermore, there are synergies between the National Post Company and the LP Entities and there is also the operational benefit of reintegrating the National Post newspaper with the other newspapers. It cannot operate independently of the services it receives from the Limited Partnership. Similarly, the LP Entities estimate that closure of the National Post would increase the LP Entities' cost burden by approximately $14 million in the fiscal year ending August 31, 2010.

[22] In its Fifth Report to the Court, the Monitor reviewed alternatives to transitioning the business of the National Post Company to the LP Entities. RBC Dominion Securities Inc. who was engaged in December, 2008 to assist in considering and evaluating recapitalization

alternatives, received no expressions of interest from parties seeking to acquire the National Post Company. Similarly, the Monitor has not been contacted by anyone interested in acquiring the business even though the need to transfer the business of the National Post Company has been in the public domain since October 6, 2009, the date of the Initial Order. The Ad Hoc Committee of Noteholders will only support the short term liquidity needs until October 30, 2009 and the National Post Company is precluded from borrowing without the Ad Hoc Committee's consent which the latter will not provide. The LP Entities will not advance funds until the transaction closes. Accordingly, failure to transition would likely result in the forced cessation of operations and the commencement of liquidation proceedings. The estimated net recovery from a liquidation range from a negative amount to an amount not materially higher than the transfer price before costs of liquidation. The senior secured creditors of the National Post Company, namely the CIT Facility lenders and Irish Holdco, support the transaction as do the members of the Ad Hoc Committee of Noteholders.

[23] The Monitor has concluded that the transaction has the following advantages over a liquidation:

- it facilitates the reorganizaton and orderly transition and subsequent termination of the shared services arrangements between the CMI Entities and the LP Entities;
- it preserves approximately 277 jobs in an already highly distressed newspaper publishing industry;
- it will help maintain and promote competition in the national daily newspaper market for the benefit of Canadian consumers; and
- the Transferee will assume substantially all of the National Post Company's trade payables (including those owed to various suppliers) and various employment costs associated with the transferred employees.

Issues

[24] The issues to consider are whether:

(a) the transfer of the assets and business of the National Post is subject to the requirements of section 36 of the *CCAA;*

(b) the Transition and Reorganization Agreement should be approved by the Court; and

(c) the stay should be extended to January 22, 2010.

Discussion

(a) Section 36 of the *CCAA*

[25] Section 36 of the *CCAA* was added as a result of the amendments which came into force on September 18, 2009. Counsel for the CMI Entities and the Monitor outlined their positions on the impact of the recent amendments to the *CCAA* on the motion before me. As no one challenged the order requested, no opposing arguments were made.

[26] Court approval is required under section 36 if:

(a) a debtor company under CCAA protection

(b) proposes to sell or dispose of assets outside the ordinary course of business.

[27] Court approval under this section of the Act[1] is only required if those threshold requirements are met. If they are met, the court is provided with a list of non-exclusive factors to consider in determining whether to approve the sale or disposition. Additionally, certain mandatory criteria must be met for court approval of a sale or disposition of assets to a related party. Notice is to be given to secured creditors likely to be affected by the proposed sale or disposition. The court may only grant authorization if satisfied that the company can and will make certain pension and employee related payments.

[28] Specifically, section 36 states:

[1] Court approval may nonetheless be required by virtue of the terms of the Initial or other court order or at the request of a stakeholder.

(1) Restriction on disposition of business assets - A debtor company in respect of which an order has been made under this Act may not sell or otherwise dispose of assets outside the ordinary course of business unless authorized to do so by a court. Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained.

(2) Notice to creditors - A company that applies to the court for an authorization is to give notice of the application to the secured creditors who are likely to be affected by the proposed sale or disposition.

(3) Factors to be considered - In deciding whether to grant the authorization, the court is to consider, among other things,

(*a*) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;

(*b*) whether the monitor approved the process leading to the proposed sale or disposition;

(*c*) whether the monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;

(*d*) the extent to which the creditors were consulted;

(*e*) the effects of the proposed sale or disposition on the creditors and other interested parties; and

(*f*) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

(4) Additional factors — related persons - If the proposed sale or disposition is to a person who is related to the company, the court may, after considering the factors referred to in subsection (3), grant the authorization only if it is satisfied that

(*a*) good faith efforts were made to sell or otherwise dispose of the assets to persons who are not related to the company; and

(*b*) the consideration to be received is superior to the consideration that would be received under any other offer made in accordance with the process leading to the proposed sale or disposition.

(5) Related persons - For the purpose of subsection (4), a person who is related to the company includes

(*a*) a director or officer of the company;

(*b*) a person who has or has had, directly or indirectly, control in fact of the company; and

(*c*) a person who is related to a person described in paragraph (*a*) or (*b*).

(6) Assets may be disposed of free and clear - The court may authorize a sale or disposition free and clear of any security, charge or other restriction and, if it does, it shall also order that other assets of the company or the proceeds of the sale or disposition be subject to a security, charge or other restriction in favour of the creditor whose security, charge or other restriction is to be affected by the order.

(7) Restriction — employers - The court may grant the authorization only if the court is satisfied that the company can and will make the payments that would have been required under paragraphs 6(4)(*a*) and (5)(*a*) if the court had sanctioned the compromise or arrangement.[2]

[29] While counsel for the CMI Entities states that the provisions of section 36 have been satisfied, he submits that section 36 is inapplicable to the circumstances of the transfer of the assets and business of the National Post Company because the threshold requirements are not met. As such, the approval requirements are not triggered. The Monitor supports this position.

[30] In support, counsel for the CMI Entities and for the Monitor firstly submit that section 36(1) makes it clear that the section only applies to a debtor company. The terms "debtor company" and "company" are defined in section 2(1) of the *CCAA* and do not expressly include a partnership. The National Post Company is a general partnership and therefore does not fall within the definition of debtor company. While I acknowledge these facts, I do not accept this argument in the circumstances of this case. Relying on case law and exercising my inherent jurisdiction, I extended the scope of the Initial Order to encompass the National Post Company and the other partnerships such that they were granted a stay and other relief. In my view, it would be inconsistent and artificial to now exclude the business and assets of those partnerships from the ambit of the protections contained in the statute.

[31] The CMI Entities' and the Monitor's second argument is that the Transition and Reorganization Agreement represents an internal corporate reorganization that is not subject to the requirements of section 36. Section 36 provides for court approval where a debtor under

[2] The reference to paragraph 6(4)a should presumably be 6(6)a.

CCAA protection proposes to sell or otherwise dispose of assets "outside the ordinary course of business". This implies, so the argument goes, that a transaction that is in the ordinary course of business is not captured by section 36. The Transition and Reorganization Agreement is an internal corporate reorganization which is in the ordinary course of business and therefore section 36 is not triggered state counsel for the CMI Entities and for the Monitor. Counsel for the Monitor goes on to submit that the subject transaction is but one aspect of a larger transaction. Given the commitments and agreements entered into with the Ad Hoc Committee of Noteholders and the Bank of Nova Scotia as agent for the senior secured lenders to the LP Entities, the transfer cannot be treated as an independent sale divorced from its rightful context. In these circumstances, it is submitted that section 36 is not engaged.

[32] The *CCAA* is remedial legislation designed to enable insolvent companies to restructure. As mentioned by me before in this case, the amendments do not detract from this objective. In discussing section 36, the Industry Canada Briefing Book[3] on the amendments states that "The reform is intended to provide the debtor company with greater flexibility in dealing with its property while limiting the possibility of abuse."[4]

[33] The term "ordinary course of business" is not defined in the *CCAA* or in the *Bankruptcy and Insolvency Act*[5]. As noted by Cullity J. in *Millgate Financial Corp. v. BCED Holdings Ltd.*[6], authorities that have considered the use of the term in various statutes have not provided an exhaustive definition. As one author observed in a different context, namely the *Bulk Sales Act*[7], courts have typically taken a common sense approach to the term "ordinary course of business" and have considered the normal business dealings of each particular seller[8]. In *Pacific Mobile Corp.*[9], the Supreme Court of Canada stated:

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[3] Industry Canada "Bill C-55: Clause by Clause Analysis—Bill Clause No. 131—CCAA Section 36".
[4] Ibid.
[5] R.S.C. 1985, c.C-36 as amended.
[6] (2003), 47 C.B.R. (4th) 278 at para.52.
[7] R.S.O. 1990, c. B. 14, as amended.
[8] D.J. Miller "Remedies under the Bulk Sales Act: (Necessary, or a Nuisance?)", Ontario Bar Association, October, 2007.
[9] [1985] 1 S.C.R. 290.

> It is not wise to attempt to give a comprehensive definition of the term "ordinary course of business" for all transactions. Rather, it is best to consider the circumstances of each case and to take into account the type of business carried on by the debtor and creditor.
>
> We approve of the following passage from Monet J.A.'s reasons discussing the phrase "ordinary course of business"…
>
> 'It is apparent from these authorities, it seems to me, that the concept we are concerned with is an abstract one and that it is the function of the courts to consider the circumstances of each case in order to determine how to characterize a given transaction. This in effect reflects the constant interplay between law and fact.'

[34] In arguing that section 36 does not apply to an internal corporate reorganization, the CMI Entities rely on the commentary of Industry Canada as being a useful indicator of legislative intent and descriptive of the abuse the section was designed to prevent. That commentary suggests that section 36(4),which deals with dispositions of assets to a related party, was intended to:

> …prevent the possible abuse by "phoenix corporations". Prevalent in small business, particularly in the restaurant industry, phoenix corporations are the result of owners who engage in serial bankruptcies. A person incorporates a business and proceeds to cause it to become bankrupt. The person then purchases the assets of the business at a discount out of the estate and incorporates a "new" business using the assets of the previous business. The owner continues their original business basically unaffected while creditors are left unpaid.[10]

[35] In my view, not every internal corporate reorganization escapes the purview of section 36. Indeed, a phoenix corporation to one may be an internal corporate reorganization to another. As suggested by the decision in *Pacific Mobile Corp*[11]., a court should in each case examine the circumstances of the subject transaction within the context of the business carried on by the debtor.

[36] In this case, the business of the National Post Company and the CP Entities are highly integrated and interdependent. The Canwest business structure predated the insolvency of the CMI Entities and reflects in part an anomaly that arose as a result of an income trust structure driven by tax considerations. The Transition and Reorganization Agreement is an internal

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[10] Supra, note 3.

reorganization transaction that is designed to realign shared services and assets within the Canwest corporate family so as to rationalize the business structure and to better reflect the appropriate business model. Furthermore, the realignment of the shared services and transfer of the assets and business of the National Post Company to the publishing side of the business are steps in the larger reorganization of the relationship between the CMI Entities and the LP Entities. There is no ability to proceed with either the Shared Services Agreement or the National Post Transition Agreement alone. The Transition and Reorganization Agreement provides a framework for the CMI Entities and the LP Entities to properly restructure their inter-entity arrangements for the benefit of their respective stakeholders. It would be commercially unreasonable to require the CMI Entities to engage in the sort of third party sales process contemplated by section 36(4) and offer the National Post for sale to third parties before permitting them to realign the shared services arrangements. In these circumstances, I am prepared to accept that section 36 is inapplicable.

(b) Transition and Reorganization Agreement

[37] As mentioned, the Transition and Reorganization Agreement is by its terms subject to court approval. The court has a broad jurisdiction to approve agreements that facilitate a restructuring: *Re Stelco Inc*.[12] Even though I have accepted that in this case section 36 is inapplicable, court approval should be sought in circumstances where the sale or disposition is to a related person and there is an apprehension that the sale may not be in the ordinary course of business. At that time, the court will confirm or reject the ordinary course of business characterization. If confirmed, at minimum, the court will determine whether the proposed transaction facilitates the restructuring and is fair. If rejected, the court will determine whether the proposed transaction meets the requirements of section 36. Even if the court confirms that the proposed transaction is in the ordinary course of business and therefore outside the ambit of section 36, the provisions of the section may be considered in assessing fairness.

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[11] Supra, note 9.
[12] (2005), 15 C.B.R. (5th) 288 (Ont. C.A.).

[38] I am satisfied that the proposed transaction does facilitate the restructuring and is fair and that the Transition and Reorganization Agreement should be approved. In this regard, amongst other things, I have considered the provisions of section 36. I note the following. The CMI recapitalization transaction which prompted the Transition and Reorganization Agreement is designed to facilitate the restructuring of CMI into a viable and competitive industry participant and to allow a substantial number of the businesses operated by the CMI Entities to continue as going concerns. This preserves value for stakeholders and maintains employment for as many employees of the CMI Entities as possible. The Transition and Reorganization Agreement was entered into after extensive negotiation and consultation between the CMI Entities, the LP Entities, their respective financial and legal advisers and restructuring advisers, the Ad Hoc Committee and the LP senior secured lenders and their respective financial and legal advisers. As such, while not every stakeholder was included, significant interests have been represented and in many instances, given the nature of their interest, have served as proxies for unrepresented stakeholders. As noted in the materials filed by the CMI Entities, the National Post Transition Agreement provides for the transfer of assets and certain liabilities to the publishing side of the Canwest business and the assumption of substantially all of the operating liabilities by the Transferee. Although there is no guarantee that the Transferee will ultimately be able to meet its liabilities as they come due, the liabilities are not stranded in an entity that will have materially fewer assets to satisfy them.

[39] There is no prejudice to the major creditors of the CMI Entities. Indeed, the senior secured lender, Irish Holdco., supports the Transition and Reorganization Agreement as does the Ad Hoc Committee and the senior secured lenders of the LP Entities. The Monitor supports the Transition and Reorganization Agreement and has concluded that it is in the best interests of a broad range of stakeholders of the CMI Entities, the National Post Company, including its employees, suppliers and customers, and the LP Entities. Notice of this motion has been given to secured creditors likely to be affected by the order.

[40] In the absence of the Transition and Reorganization Agreement, it is likely that the National Post Company would be required to shut down resulting in the consequent loss of employment for most or all the National Post Company's employees. Under the National Post

Transition Agreement, all of the National Post Company employees will be offered employment and as noted in the affidavit of the moving parties, the National Post Company's obligations and liabilities under the pension plan will be assumed, subject to necessary approvals.

[41] No third party has expressed any interest in acquiring the National Post Company. Indeed, at no time did RBC Dominion Securities Inc. who was assisting in evaluating recapitalization alternatives ever receive any expression of interest from parties seeking to acquire it. Similarly, while the need to transfer the National Post has been in the public domain since at least October 6, 2009, the Monitor has not been contacted by any interested party with respect to acquiring the business of the National Post Company. The Monitor has approved the process leading to the sale and also has conducted a liquidation analysis that caused it to conclude that the proposed disposition is the most beneficial outcome. There has been full consultation with creditors and as noted by the Monitor, the Ad Hoc Committee serves as a good proxy for the unsecured creditor group as a whole. I am satisfied that the consideration is reasonable and fair given the evidence on estimated liquidation value and the fact that there is no other going concern option available.

[42] The remaining section 36 factor to consider is section 36(7) which provides that the court should be satisfied that the company can and will make certain pension and employee related payments that would have been required if the court had sanctioned the compromise or arrangement. In oral submissions, counsel for the CMI Entities confirmed that they had met the requirements of section 36. It is agreed that the pension and employee liabilities will be assumed by the Transferee. Although present, the representative of the Superintendent of Financial Services was unopposed to the order requested. If and when a compromise and arrangement is proposed, the Monitor is asked to make the necessary inquiries and report to the court on the status of those payments.

Stay Extension

[43] The CMI Entities are continuing to work with their various stakeholders on the preparation and filing of a proposed plan of arrangement and additional time is required. An extension of the stay of proceedings is necessary to provide stability during that time. The cash

flow forecast suggests that the CMI Entities have sufficient available cash resources during the requested extension period. The Monitor supports the extension and nobody was opposed. I accept the statements of the CMI Entities and the Monitor that the CMI Entities have acted, and are continuing to act, in good faith and with due diligence. In my view it is appropriate to extend the stay to January 22, 2010 as requested.

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Pepall J.

Released: November 12, 2009

Tab 4

Attorney General of Canada *Appellant*

v.

Fairmont Hotels Inc., FHIW Hotel Investments (Canada) Inc. and FHIS Hotel Investments (Canada) Inc. *Respondents*

Indexed as: Canada (Attorney General) *v.* Fairmont Hotels Inc.

2016 SCC 56

File No.: 36606.

2016: May 18; 2016: December 9.

Present: McLachlin C.J. and Abella, Cromwell, Moldaver, Karakatsanis, Wagner, Gascon, Côté and Brown JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Contracts — Equity — Remedies — Rectification of written instrument recording prior agreement — Agreement intended by parties to operate on tax-neutral basis — Corporate resolutions effecting share redemption — Share redemption having unintended tax consequences — Whether courts below erred in holding parties' intention can support grant of rectification — Whether equitable remedy of rectification available.

Commercial law — Corporations — Taxation — Whether rectification of contract amounts to retroactive tax planning.

Fairmont Hotels Inc. was involved in the financing of Legacy Hotels' purchase of two other hotels, in U.S. currency. The financing arrangement was intended to operate on a tax-neutral basis. When Fairmont was later acquired, that intention was frustrated, however, since the acquisition would cause Fairmont and its subsidiaries to realize a deemed foreign exchange loss. The parties to Fairmont's acquisition therefore agreed on a plan, which allowed Fairmont to hedge itself against any exposure to the foreign exchange tax liability, but not its subsidiaries. There was no plan for protecting them from such exposure because the plan was deferred. The following year, Legacy Hotels asked Fairmont to terminate their financing arrangement to allow for the sale of the two other hotels. Therefore, Fairmont redeemed its shares in

Procureur général du Canada *Appelant*

c.

Hôtels Fairmont Inc., FHIW Hotel Investments (Canada) Inc. et FHIS Hotel Investments (Canada) Inc. *Intimées*

Répertorié : Canada (Procureur général) *c.* Hôtels Fairmont Inc.

2016 CSC 56

N° du greffe : 36606.

2016 : 18 mai; 2016 : 9 décembre.

Présents : La juge en chef McLachlin et les juges Abella, Cromwell, Moldaver, Karakatsanis, Wagner, Gascon, Côté et Brown.

EN APPEL DE LA COUR D'APPEL DE L'ONTARIO

Contrats — Equity — Recours — Rectification d'un instrument écrit qui consigne une entente antérieure — Souhait des parties que l'entente soit exécutée de façon neutre sur le plan fiscal — Résolutions d'une société portant rachat d'actions — Rachat d'actions entraînant des conséquences non souhaitées — Les juridictions inférieures ont-elles commis une erreur en concluant que l'intention des parties peut justifier l'octroi d'une rectification? — Est-il possible d'obtenir la rectification, une réparation en equity?

Droit commercial — Sociétés par actions — Fiscalité — La rectification du contrat est-elle assimilable à une planification fiscale rétroactive?

Hôtels Fairmont Inc. a participé au financement de l'acquisition, par Legacy Hotels, de deux autres hôtels en dollars américains. L'entente de financement devait être exécutée de façon neutre sur le plan fiscal. Lorsque Fairmont a été acquise par la suite, cet objectif a toutefois été contrecarré, puisque l'acquisition aurait fait subir à Fairmont et à ses filiales une perte sur change présumée. Les parties à l'acquisition de Fairmont ont donc convenu d'un plan qui permettait à Fairmont, mais non à ses filiales, de se protéger du risque d'être tenue à une obligation fiscale prospective sur les opérations de change. Aucun plan n'a été échafaudé pour protéger les filiales de ce risque parce que la conception de ce plan a été reportée à plus tard. L'année suivante, Legacy Hotels a demandé à Fairmont de résilier leur entente de financement

its subsidiaries, by resolutions passed by their directors. This resulted however in an unanticipated tax liability. Fairmont sought to avoid that liability by rectification of the directors' resolutions. Both the application judge and the Court of Appeal granted that rectification on the basis of the parties' intended tax neutrality.

Held (Abella and Côté JJ. dissenting): The appeal should be allowed.

Per McLachlin C.J. and Cromwell, Moldaver, Karakatsanis, Wagner, Gascon and Brown JJ.: Both courts below erred in holding that the parties' intention of tax neutrality could support a grant of rectification. A common continuing intention does not suffice. Rectification is an equitable remedy designed to correct errors in the recording of terms in written legal instruments. It is limited to cases where a written instrument has incorrectly recorded the parties' antecedent agreement. In other words, rectification is not available where the basis for seeking it is that one or both of the parties wish to amend not the instrument recording their agreement, but the agreement itself.

Where the error is said to result from a mistake common to both or all parties to the agreement, rectification of the instrument is available upon the court being satisfied that there was a prior agreement whose terms are definite and ascertainable; that the agreement was still in effect at the time the instrument was executed; that the instrument fails to accurately record the agreement; and that the instrument, if rectified, would carry out the parties' prior agreement.

It falls to a party seeking rectification to show not only the putative error in the instrument, but also the way in which the instrument should be rectified in order to correctly record what the parties intended to do. The applicable standard of proof to be applied to evidence adduced in support of a grant of rectification is the balance of probabilities. A court will typically require evidence exhibiting a high degree of clarity, persuasiveness and cogency before substituting the terms of a written instrument with those said to form the parties' true intended course of action. On rectification, both equity and the civil law are *ad idem*, despite each legal system arriving at it by different paths — the former being concerned with correcting the document, and the latter focusing on

de façon à permettre la vente des deux autres hôtels. Par conséquent, Fairmont a racheté les actions qu'elle détenait dans ses filiales au moyen de résolutions adoptées par leurs administrateurs. Cette opération a toutefois fait naître une obligation fiscale imprévue. Fairmont a voulu se soustraire à cette obligation en faisant rectifier les résolutions des administrateurs. Tant le juge saisi de la demande que la Cour d'appel ont accordé cette rectification au motif que les parties recherchaient la neutralité fiscale.

Arrêt (les juges Abella et Côté sont dissidentes) : Le pourvoi est accueilli.

La juge en chef McLachlin et les juges Cromwell, Moldaver, Karakatsanis, Wagner, Gascon et Brown : Les deux juridictions inférieures ont commis une erreur en concluant que l'objectif de neutralité fiscale des parties pouvait justifier l'octroi d'une rectification. Une intention commune constante ne suffit pas. La rectification est une réparation en equity visant à corriger les erreurs dans la consignation de modalités dans des instruments juridiques écrits. Il n'y a rectification que dans les cas où un instrument écrit a consigné incorrectement l'entente antérieure entre les parties. Autrement dit, la rectification ne peut être accordée lorsqu'elle est fondée sur le désir de l'une des parties ou des deux de modifier non pas l'instrument consignant leur entente, mais l'entente elle-même.

Lorsqu'on allègue que l'erreur résulte d'une erreur commune à toutes les parties à l'entente, le tribunal peut accorder la rectification de l'instrument s'il est convaincu qu'il y avait une entente antérieure dont les modalités sont déterminées et déterminables, que l'entente était toujours en vigueur au moment de la signature de l'instrument, que l'instrument ne consigne pas correctement l'entente et que l'instrument, s'il est rectifié, exécuterait l'entente antérieure des parties.

Il incombe à la partie qui sollicite la rectification de démontrer non seulement l'erreur putative, mais également la façon dont l'instrument devrait être rectifié afin de consigner correctement ce que les parties avaient l'intention de faire. La norme de preuve applicable à la preuve présentée à l'appui d'une demande de rectification est la prépondérance des probabilités. Le tribunal exigera généralement une preuve très claire, convaincante et solide avant de permettre que les modalités d'un instrument écrit soient remplacées par celles qui constateraient la véritable intention des parties. En matière de rectification, l'equity et le droit civil vont dans le même sens, malgré le fait que chaque système juridique arrive à une même conclusion par des voies différentes — le

its interpretation. This convergence is undoubtedly desirable.

These principles are to be applied in a tax context just as they are in a non-tax context. This is to avoid impermissible retroactive tax planning. In this case, the application of these principles leads unavoidably to the conclusion that Fairmont's application for rectification should have been dismissed, since it could not demonstrate having reached a prior agreement with definite and ascertainable terms. It is clear that Fairmont intended to limit, if not avoid altogether, its tax liability in unwinding the financing arrangement. And, by redeeming the shares, this intention was frustrated. Without more, however, these facts do not support a grant of rectification. Rectification is not equity's version of a mulligan. Courts rectify instruments that do not correctly record agreements. Courts do not rectify agreements where their faithful recording in an instrument has led to an undesirable or otherwise unexpected outcome.

Relatedly, Fairmont has not demonstrated how its intention, held in common and on a continuing basis with its subsidiaries, was to be achieved in definite and ascertainable terms while unwinding the financing arrangement. Fairmont refers to a plan to protect its subsidiaries from foreign exchange tax liability, but that plan was not only imprecise. It really was not a plan at all, being at best an inchoate wish to protect the subsidiaries, by unspecified means.

Per Abella and Côté JJ. (dissenting): There is no adjustment to the test for rectification in a tax case, and in this case the test has been met. The lower court's decisions to grant rectification resulted from the factual finding that the parties had a continuing, ascertainable intention to pursue the transaction on a tax-free basis or not at all. The majority's approach however unduly narrows the doctrine of rectification's scope. A common, continuing, definite and ascertainable intention to pursue a transaction in a tax-neutral manner has usually satisfied the threshold for granting rectification. The additional requirement that the parties clearly identify the precise mechanism by which they intended to achieve tax neutrality, and how that mechanism was mistakenly transcribed in a document, has the effect of raising the threshold and frustrating the purpose of the remedy. Whether a mistake is unilateral or mutual, rectification is, ultimately, an equitable remedy that seeks to give effect to the true intention of the parties, and prevent errors

premier visant la correction du document, et le dernier étant axé sur son interprétation. Cette convergence est indubitablement souhaitable.

Ces principes doivent être appliqués dans un contexte fiscal exactement de la même manière que dans un contexte non fiscal afin d'éviter une planification fiscale rétroactive inadmissible. En l'espèce, l'application de ces principes mène inévitablement à la conclusion que la demande de rectification de Fairmont aurait dû être rejetée, puisqu'elle n'a pu démontrer qu'elle avait conclu une entente antérieure dont les modalités étaient déterminées et déterminables. Il est clair que Fairmont comptait limiter, voire éviter complètement, son obligation fiscale en annulant l'entente de financement. Et le rachat des actions a contrecarré cette intention. Sans plus, toutefois, ces faits ne justifient pas l'octroi d'une rectification. La rectification n'est pas équivalente en equity à un second essai. Les tribunaux rectifient des instruments qui ne consignent pas correctement une entente. Ils ne rectifient pas les ententes dont la consignation fidèle dans un instrument a mené à un résultat indésirable ou par ailleurs imprévu.

De même, Fairmont n'a pas démontré comment son intention, qu'elle partageait de manière constante avec ses filiales, devait être réalisée selon des modalités déterminées et déterminables tout en annulant l'entente de financement. Fairmont parle d'un plan visant à protéger ses filiales contre une obligation fiscale sur les opérations de change, mais ce plan n'était pas seulement imprécis. Il ne s'agissait même pas en fait d'un plan. Ce n'était tout au plus qu'un désir incomplet de protéger les filiales par des moyens non précisés.

Les juges Abella et Côté (dissidentes) : Il n'y a pas lieu de modifier le test de rectification dans une affaire de nature fiscale et, en l'espèce, ce test a été respecté. Les décisions des juridictions inférieures d'accorder la rectification reposent sur la conclusion de fait que les parties avaient l'intention constante et déterminable de réaliser l'opération sans incidences fiscales, ou de ne pas la réaliser du tout. L'approche de la majorité restreint toutefois indûment la portée de la doctrine de la rectification. L'intention commune, constante, déterminée et déterminable de réaliser une opération sans incidences fiscales satisfait habituellement au seuil d'octroi d'une rectification. L'exigence supplémentaire selon laquelle les parties doivent désigner clairement le mécanisme précis au moyen duquel elles ont l'intention d'atteindre la neutralité fiscale, ainsi que la manière dont ce mécanisme a été incorrectement transcrit dans le document, a pour effet de hausser le seuil et de contrecarrer l'objet de la réparation. Que l'erreur soit unilatérale ou commune,

from causing windfalls. The doctrine is also based on the principle of unjust enrichment, namely, that it would be unfair to rigidly enforce an error that enriches one party at the expense of another.

While rectification seems most often to have been granted in the context of agreed upon terms having been transcribed incorrectly, since unjust enrichment can result from a mistake in carrying out the intention of the parties, the remedy is also available to correct errors in implementation. Courts have, as a result, granted rectification where a corporate transaction was conducted in the wrong sequence, where an underlying calculation in a contract was incorrect, and where the requisite steps of an amalgamation were not correctly carried out.

Whether the errors are in transcription or in implementation, courts may refuse to exercise their discretion where allowing rectification would prejudice the rights of third parties. But the mere existence of a third party will not bar rectification. Only where the third party has actually relied on the flawed agreement will rectification be barred. Just as rectification can prevent one party from enforcing an error and being unjustly enriched by the other's mistake, rectification can also prevent a third party who has not relied on the agreement from enforcing a mistake and receiving a windfall.

Allowing the tax authorities, a third party, to profit from legitimate tax planning errors, when its own rights have not been prejudiced in any way, amounts to unjust enrichment. Businesses and individuals are legally entitled to structure their affairs in a way that minimizes their tax burden. The tax department is not entitled to play "Gotcha" any more than would any other third party who did not rely to its detriment on the mistake. On the other hand, businesses and individuals should not be allowed to exploit rectification for purposes of engaging in retroactive tax planning.

Civil law and common law rectification in the tax context are clearly based on analogous principles, namely, that the true intention of the parties has primacy over errors in the transcription or implementation of that agreement, subject to a need for precision and the rights of third parties who detrimentally rely on the agreement. That means that there is no principled basis in either legal system for a stricter standard in the tax context simply

la rectification est, en définitive, une réparation d'equity qui vise à donner effet à la véritable intention des parties et à empêcher que des erreurs donnent lieu à des gains fortuits. La doctrine est aussi fondée sur le principe d'enrichissement injustifié, à savoir qu'il serait injuste de donner effet, de façon rigide, à une erreur qui enrichit l'une des parties au détriment de l'autre.

Certes, on semble avoir le plus souvent accordé la rectification dans des cas où les modalités convenues avaient été mal transcrites, mais puisque l'enrichissement injustifié peut résulter d'une erreur dans la réalisation de l'intention des parties, on peut aussi recourir à la rectification pour corriger les erreurs de mise en œuvre. Les tribunaux ont donc accordé la rectification demandée lorsqu'une transaction commerciale a été exécutée dans le mauvais ordre, lorsqu'une erreur de calcul sous-jacente au contrat a été commise, et lorsque les étapes nécessaires d'une fusion ont été mal suivies.

Que l'erreur réside dans la transcription ou dans la mise en œuvre, les tribunaux peuvent refuser d'exercer leur pouvoir discrétionnaire si la rectification serait préjudiciable aux droits des tiers. Toutefois, la simple présence d'un tiers ne fait pas obstacle à la rectification. La rectification ne sera irrecevable que si le tiers en question s'est effectivement fondé sur l'entente erronée. La rectification peut empêcher une partie de donner effet à une erreur et de s'enrichir injustement parce que l'autre partie s'est trompée, tout comme elle peut empêcher un tiers qui ne s'est pas fié sur l'entente de donner effet à une erreur et d'en tirer profit.

Permettre aux autorités fiscales, une tierce partie, de tirer profit des erreurs commises dans une planification fiscale légitime, alors qu'il n'a été nullement porté atteinte à ses droits, équivaut à un enrichissement injustifié. Les entreprises et les particuliers ont légalement le droit d'organiser leurs affaires de manière à réduire le plus possible leur fardeau fiscal. Le fisc ne peut pas plus jouer à « *Gotcha* » que n'importe quel autre tiers qui ne s'est pas fondé à son détriment sur l'erreur. D'autre part, les entreprises et les particuliers ne devraient pas pouvoir recourir à la rectification pour procéder à une planification fiscale rétroactive.

La rectification en droit civil et celle en common law dans le domaine fiscal sont manifestement fondées sur des principes analogues, à savoir que la véritable intention des parties l'emporte sur les erreurs de transcription ou de mise en œuvre de l'entente en question, sous réserve des précisions nécessaires et des droits des tiers qui se fondent à leur détriment sur l'entente. Ainsi, aucune raison de principe ne permet, quel que soit le système

because it is the government that is positioned to benefit from a mistake.

In this case, Fairmont was found by the application judge to have always had a clear, continuing intention to unwind the financing arrangement on a tax-neutral basis and never to redeem the shares. Fairmont was not attempting to change its original intention because of unanticipated tax consequences. It had anticipated the tax consequences of unwinding the arrangement with a share redemption mechanism, and it specifically rejected this course of action. But, by mistake, the preferred share redemption terms were included in the directors' resolutions. This is exactly the kind of mistake rectification exists to remedy. Once the application judge was satisfied of the true intention of the parties, he was entitled to give effect to it by allowing rectification of the directors' resolutions.

To require an exhaustive account of how the unwinding was supposed to have proceeded would amount to imposing a uniquely high threshold for rectification in the tax context and would give the Canada Revenue Agency, as the tax authorities, an unintended gain because of the mistake. There is no basis for permitting a windfall to the Canada Revenue Agency that no other third party would have been entitled to.

Cases Cited

By Brown J.

Overruled: *Juliar v. Canada (Attorney General)* (1999), 46 O.R. (3d) 104, aff'd (2000), 50 O.R. (3d) 728; **considered:** *Joscelyne v. Nissen*, [1970] 2 Q.B. 86; **referred to:** *Shafron v. KRG Insurance Brokers (Western) Inc.*, 2009 SCC 6, [2009] 1 S.C.R. 157; *Performance Industries Ltd. v. Sylvan Lake Golf & Tennis Club Ltd.*, 2002 SCC 19, [2002] 1 S.C.R. 678; *Mackenzie v. Coulson* (1869), L.R. 8 Eq. 368; *Ship M. F. Whalen v. Pointe Anne Quarries Ltd.* (1921), 63 S.C.R. 109; *Hart v. Boutilier* (1916), 56 D.L.R. 620; *Re Slocock's Will Trusts*, [1979] 1 All E.R. 358; *Racal Group Services Ltd. v. Ashmore* (1995), 68 T.C. 86; *Ashcroft v. Barnsdale*, [2010] EWHC 1948, [2010] S.T.C. 2544; *Shell Canada Ltd. v. Canada*, [1999] 3 S.C.R. 622; *Harvest Operations Corp. v. Canada (Attorney General)*, 2015 ABQB 327, [2015] 6 C.T.C. 78; *Crane v. Hegeman-Harris Co.*, [1939] 1 All E.R. 662; *Wasauksing First Nation v. Wasausink Lands Inc.* (2004), 184 O.A.C. 84; *Dynamex Canada Inc. v. Miller* (1998), 161 Nfld. & P.E.I.R. 97; *Frederick E. Rose (London) Ld. v. William H. Pim Jnr. & Co.*, [1953] 2

juridique applicable, d'imposer une norme plus stricte dans le domaine fiscal du simple fait que c'est le gouvernement qui pourrait bénéficier d'une erreur.

En l'espèce, le juge saisi de la demande a conclu que Fairmont avait toujours eu l'intention claire de dénouer l'entente de financement sans incidences fiscales et n'avait jamais eu l'intention de racheter les actions. Fairmont ne tentait pas de s'écarter de son intention initiale à cause de conséquences fiscales imprévues. Elle avait prévu les conséquences fiscales d'un dénouement de l'arrangement par le rachat des actions, et elle avait explicitement rejeté cette démarche. Or, par erreur, les modalités de rachat des actions privilégiées ont été incluses dans les résolutions adoptées par les administrateurs. C'est exactement le genre d'erreur que la rectification vise à corriger. Une fois que le juge saisi de la demande a été convaincu de la véritable intention des parties, il avait le droit de lui donner effet en autorisant la rectification des résolutions des administrateurs.

Exiger une description détaillée de la manière dont le dénouement était censé se dérouler reviendrait à imposer un seuil exceptionnellement élevé à atteindre pour obtenir la rectification dans le domaine fiscal et permettrait à l'Agence du revenu du Canada, les autorités fiscales, de tirer un gain fortuit de l'erreur. Il n'y a aucune raison de permettre à l'Agence du revenu du Canada de tirer un gain fortuit auquel aucun autre tiers n'aurait eu droit.

Jurisprudence

Citée par le juge Brown

Arrêt renversé : *Juliar c. Canada (Attorney General)* (1999), 46 O.R. (3d) 104, conf. par (2000), 50 O.R. (3d) 728; **arrêt examiné :** *Joscelyne c. Nissen*, [1970] 2 Q.B. 86; **arrêts mentionnés :** *Shafron c. KRG Insurance Brokers (Western) Inc.*, 2009 CSC 6, [2009] 1 R.C.S. 157; *Performance Industries Ltd. c. Sylvan Lake Golf & Tennis Club Ltd.*, 2002 CSC 19, [2002] 1 R.C.S. 678; *Mackenzie c. Coulson* (1869), L.R. 8 Eq. 368; *Ship M. F. Whalen c. Pointe Anne Quarries Ltd.* (1921), 63 R.C.S. 109; *Hart c. Boutilier* (1916), 56 D.L.R. 620; *Re Slocock's Will Trusts*, [1979] 1 All E.R. 358; *Racal Group Services Ltd. c. Ashmore* (1995), 68 T.C. 86; *Ashcroft c. Barnsdale*, [2010] EWHC 1948, [2010] S.T.C. 2544; *Shell Canada Ltée c. Canada*, [1999] 3 R.C.S. 622; *Harvest Operations Corp. c. Canada (Attorney General)*, 2015 ABQB 327, [2015] 6 C.T.C. 78; *Crane c. Hegeman-Harris Co.*, [1939] 1 All E.R. 662; *Wasauksing First Nation c. Wasausink Lands Inc.* (2004), 184 O.A.C. 84; *Dynamex Canada Inc. c. Miller* (1998), 161 Nfld. & P.E.I.R. 97; *Frederick E. Rose (London) Ld. c. William H. Pim Jnr. & Co.*, [1953]

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By Abella J. (dissenting)

H. F. Clarke Ltd. v. Thermidaire Corp., [1973] 2 O.R. 57, rev'd [1976] 1 S.C.R. 319; *Performance Industries Ltd. v. Sylvan Lake Golf & Tennis Club Ltd.*, 2002 SCC 19, [2002] 1 S.C.R. 678; *Hart v. Boutilier* (1916), 56 D.L.R. 620; *Mitchell v. MacMillan* (1980), 5 Sask. R. 160; *Reed Shaw Osler Ltd. v. Wilson* (1981), 17 Alta. L.R. (2d) 81; *Bryndon Ventures Inc. v. Bragg* (1991), 82 D.L.R. (4th) 383; *Dynamex Canada Inc. v. Miller* (1998), 161 Nfld. & P.E.I.R. 97; *Wasauksing First Nation v. Wasausink Lands Inc.* (2004), 184 O.A.C. 84; *Joscelyne v. Nissen*, [1970] 2 Q.B. 86; *Peter Pan Drive-In Ltd. v. Flambro Realty Ltd.* (1978), 22 O.R. (2d) 291, aff'd (1980), 26 O.R. (2d) 746; *Graymar Equipment (2008) Inc. v. Canada (Attorney General)*, 2014 ABQB 154, 97 Alta. L.R. (5th) 288; *I.C.R.V. Holdings Ltd. v. Tri-Par Holdings Ltd.* (1994), 53 B.C.A.C. 72; *McLean v. McLean*, 2013 ONCA 788, 118 O.R. (3d) 216; *Swainland Builders Ltd. v. Freehold Properties Ltd.*, [2002] EWCA Civ 560; *Co-operative Insurance Society Ltd v. Centremoor Ltd.*, [1983] 2 E.G.L.R. 52; *Royal Bank of Canada v. El-Bris Ltd.*, 2008 ONCA 601, 92 O.R. (3d) 779; *Shafron v. KRG Insurance Brokers (Western) Inc.*, 2009 SCC 6, [2009] 1 S.C.R. 157; *GT Group Telecom Inc., Re* (2004), 5 C.B.R. (5th) 230; *Oriole Oil & Gas Ltd. v. American Eagle Petroleums Ltd.* (1981), 27 A.R. 411; *Prospera Credit Union, Re*, 2002 BCSC 1806, 32 B.L.R. (3d) 145; *Wise v. Axford*, [1954] O.W.N. 822; *Augdome Corp. v. Gray*, [1975] 2 S.C.R. 354; *Consortium Capital Projects Inc. v. Blind River Veneer Ltd.* (1988), 63 O.R. (2d) 761, aff'd (1990), 72 O.R. (2d) 703; *Kolias v. Owners: Condominium Plan 309 CDC*, 2008 ABCA 379, 440 A.R. 389; *Carlson, Carlson and Hettrick v. Big Bud Tractor of Canada Ltd.* (1981), 7 Sask. R. 337; *Love v. Love*, 2013 SKCA 31, [2013] 5 W.W.R. 662; *Copthorne Holdings Ltd. v. Canada*, 2011 SCC 63, [2011] 3 S.C.R. 721; *Shell Canada Ltd. v. Canada*, [1999] 3 S.C.R. 622; *Kanji v. Canada (Attorney General)*, 2013 ONSC 781, 114 O.R. (3d) 1; *Pallen Trust, Re*, 2015 BCCA 222, 385 D.L.R. (4th) 499; *771225 Ontario Inc. v. Bramco Holdings Co.* (1995), 21 O.R. (3d) 739; *Canada (Attorney General) v. Juliar* (2000), 50 O.R. (3d) 728; *McPeake v. Canada (Attorney General)*, 2012 BCSC 132, [2012] 4 C.T.C. 203; *Slate Management Corp. v. Canada (Attorney General)*, 2016 ONSC 4216;

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Geoff R. Hall and *Chia-yi Chua*, for the respondents.

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Daniel Bourgeois et *Eric Noble*, pour l'appelant.

Geoff R. Hall et *Chia-yi Chua*, pour les intimées.

The judgment of McLachlin C.J. and Cromwell, Moldaver, Karakatsanis, Wagner, Gascon and Brown JJ. was delivered by

Brown J. —

I. Introduction

[1] This appeal concerns the conditions under which a taxpayer may ask a court to exercise its equitable jurisdiction to rectify a written legal instrument, where the effect of that instrument was to produce an unexpected tax consequence. As I will explain, this entails inquiring into the nature and particularity of the terms which the taxpayer had intended to record in the instrument, whether the instrument contains those intended terms and, if not, whether those intended terms are sufficiently precise such that they may now be included in the instrument.

[2] The present case arises from a financing arrangement which the parties had intended, both at its inception and ongoing, to operate on a tax-neutral basis. Because of the particular financing mechanism chosen, an unanticipated tax liability was incurred. Both the chambers judge at the Ontario Superior Court of Justice and the Court of Appeal for Ontario granted rectification on the grounds of the parties' intended tax neutrality.

[3] Without disputing that tax neutrality was the parties' intention, for the reasons that follow it is my respectful view that both courts below erred in holding that this intention could support a grant of rectification. Rectification is limited to cases where the agreement between the parties was not correctly recorded in the instrument that became the final expression of their agreement: A. Swan and J. Adamski, *Canadian Contract Law* (3rd ed. 2012), at §8.229; M. McInnes, *The Canadian Law of Unjust Enrichment and Restitution* (2014), at p. 817. It does not undo unanticipated effects of that agreement. While, therefore, a court may rectify an instrument which inaccurately records a party's agreement respecting what was to be done, it may not change the agreement in order to salvage

Version française du jugement de la juge en chef McLachlin et des juges Cromwell, Moldaver, Karakatsanis, Wagner, Gascon et Brown rendu par

Le juge Brown —

I. Introduction

[1] Ce pourvoi porte sur les conditions régissant les situations où un contribuable peut demander au tribunal d'exercer sa compétence en equity pour rectifier un instrument juridique écrit, lorsque cet instrument a eu pour effet d'entraîner une conséquence fiscale imprévue. Comme je l'expliquerai, cela implique que l'on examine la nature et les particularités des modalités que le contribuable avait l'intention de consigner dans l'instrument, si l'instrument renferme ces modalités et, dans la négative, si ces modalités sont suffisamment précises pour qu'elles puissent maintenant être incluses dans l'instrument.

[2] Ce pourvoi découle d'une entente de financement que les parties entendaient, dès sa naissance et après, exécuter en assurant la neutralité fiscale. Le mécanisme de financement choisi a fait naître une obligation fiscale imprévue. Tant le juge siégeant en cabinet de la Cour supérieure de justice de l'Ontario que la Cour d'appel de l'Ontario ont accordé la rectification demandée au motif que les parties recherchaient la neutralité fiscale.

[3] Sans contester que la neutralité fiscale fût l'intention des parties, pour les motifs qui suivent, et soit dit en tout respect, je suis d'avis que les deux juridictions inférieures ont commis une erreur en concluant que cette intention pouvait justifier l'octroi d'une rectification. Il n'y a rectification que dans les cas où l'entente entre les parties n'a pas été correctement consignée dans l'instrument qui est devenu l'expression finale de leur entente : A. Swan et J. Adamski, *Canadian Contract Law* (3e éd. 2012), §8.229; M. McInnes, *The Canadian Law of Unjust Enrichment and Restitution* (2014), p. 817. Elle n'annule pas les effets imprévus de cette entente. Par conséquent, bien que le tribunal puisse rectifier un instrument qui consigne incorrectement l'entente conclue par une partie au sujet de ce qui

what a party hoped to achieve. Moreover, these rules confining the availability of rectification are generally applicable, including where (as here) the unanticipated effect takes the form of a tax liability. To be clear, a court may not modify an instrument merely because a party has discovered that its operation generates an adverse and unplanned tax liability. I would therefore allow the appeal.

devait être fait, il ne peut le faire pour épargner ce qu'une partie espérait obtenir. De plus, ces règles limitant la possibilité d'obtenir une rectification sont d'application générale, notamment dans les cas où (comme en l'espèce) l'effet imprévu prend la forme d'une obligation fiscale. Plus précisément, le tribunal ne peut modifier un instrument simplement parce qu'une partie a découvert que son exécution fait naître une obligation fiscale préjudiciable et imprévue. Par conséquent, je suis d'avis d'accueillir le pourvoi.

II. Overview of Facts and Proceedings

A. *Background*

[4] The respondent Fairmont Hotels Inc. and its subsidiaries FHIW Hotel Investments (Canada) Inc. and FHIS Hotel Investments (Canada) Inc. ask the Court to rectify instruments recording a complex financing arrangement made in 2002 and 2003 between Fairmont and Legacy Hotels REIT, a Canadian real estate investment trust in which Fairmont owned a minority interest. While Fairmont's aim in participating in this financing arrangement was to obtain the management contract for the two hotels which Legacy purchased with the financing, its participation exposed it to a potential foreign exchange tax liability, since the financing was in U.S. currency. With the goal of ensuring foreign exchange tax neutrality, Fairmont — through its subsidiaries FHIW and FHIS — entered into reciprocal loan agreements with Legacy, all of which were transacted in U.S. currency.

[5] When Fairmont was acquired by Kingdom Hotels International and Colony Capital LLC in 2006, however, that goal of foreign exchange tax neutrality was frustrated, since this acquisition would cause Fairmont and its subsidiaries to realize a deemed foreign exchange loss, without corresponding foreign exchange gains, on the financing arrangement with Legacy. Fairmont, Kingdom Hotels and Colony Capital agreed on a "modified plan" which allowed Fairmont (but not its subsidiaries) to realize both its gains and losses in 2006, thereby fully hedging it

II. Aperçu des faits et de la procédure

A. *Contexte*

[4] L'intimée Hôtels Fairmont Inc. et ses filiales FHIW Hotel Investments (Canada) Inc. et FHIS Hotel Investments (Canada) Inc. prient la Cour de rectifier des instruments consignant une entente de financement complexe conclue en 2002 et en 2003 entre Fairmont et Legacy Hotels REIT, une fiducie canadienne d'investissement immobilier dans laquelle Fairmont détenait une participation minoritaire. Bien que le but de Fairmont en participant à cette entente de financement fût d'obtenir le contrat de gestion des deux hôtels que Legacy a acquis avec les fonds prêtés, sa participation l'a exposée à une obligation fiscale potentielle sur les opérations de change, puisque le financement était en dollars américains. Dans le but d'assurer la neutralité fiscale des opérations de change, Fairmont — par l'intermédiaire de ses filiales FHIW et FHIS — a conclu des contrats de prêts réciproques avec Legacy qui ont tous été négociés en dollars américains.

[5] Lorsque Fairmont a été acquise par Kingdom Hotels International et Colony Capital LLC en 2006, toutefois, cet objectif de neutralité fiscale des opérations de change a été contrecarré, puisque cette acquisition aurait fait subir à Fairmont et à ses filiales une perte sur change présumée, sans gains sur change correspondants, par suite de l'entente de financement conclue avec Legacy. Fairmont, Kingdom Hotels et Colony Capital ont convenu d'un [TRADUCTION] « plan modifié » qui permettait à Fairmont, mais non à ses filiales, de réaliser ses gains et ses pertes en

against exposure to prospective foreign exchange tax liability. The matter of similarly protecting the subsidiaries from exposure was deferred, without any specific plan as to how that might be achieved.

[6] In 2007, Legacy asked Fairmont to terminate the reciprocal loan arrangements "on an urgent basis" so as to allow for the sale of the hotels. Four days later, and on the incorrect assumption that the matter of the subsidiaries' foreign exchange tax neutrality had been secured, Fairmont complied with Legacy's request by redeeming its shares in its subsidiaries via resolutions passed by the directors of FHIW and FHIS. This resulted in an unanticipated tax liability, discovered only after the Canada Revenue Agency ("CRA") audited the 2007 tax returns of FHIW and FHIS and questioned Fairmont on those returns.

[7] The respondents now seek to avoid that liability to Fairmont by asking the Court to rectify the 2007 resolutions passed by the directors of FHIW and FHIS. Specifically, they wish to convert Fairmont's share redemption into a loan whereby FHIW and FHIS will loan to Fairmont the same amount that they paid to Fairmont for the share redemption.

B. *Judicial History*

(1) Superior Court of Justice — Newbould J. (2014 ONSC 7302, 123 O.R. (3d) 241)

[8] Relying on the decision of the Ontario Court of Appeal in *Juliar v. Canada (Attorney General)* (1999), 46 O.R. (3d) 104 (S.C.J.), aff'd (2000), 50 O.R. (3d) 728 (C.A.), the chambers judge allowed the application for rectification. He found that, since 2002, Fairmont had intended that its financing arrangement with Legacy be tax-neutral in effect, and that this intention subsisted after Fairmont's 2006 acquisition by Kingdom Hotels and Colony Capital (para. 32).

2006, la protégeant ainsi totalement du risque d'être tenue à une obligation fiscale prospective sur les opérations de change. L'idée de protéger de la même façon les filiales a été reportée à plus tard, sans plan précis quant à savoir comment elle pourrait être menée à bien.

[6] En 2007, Legacy a demandé à Fairmont de résilier [TRADUCTION] « de toute urgence » les contrats de prêts réciproques de façon à permettre la vente des hôtels. Quatre jours plus tard, et supposant à tort que la question de la neutralité fiscale des opérations de change des filiales avait été réglée, Fairmont a accédé à la demande de Legacy en rachetant les actions qu'elle détenait dans ses filiales au moyen de résolutions adoptées par les administrateurs de FHIW et de FHIS. Cette opération a fait naître une obligation fiscale imprévue, découverte seulement après que l'Agence du revenu du Canada (« ARC ») eut vérifié les déclarations de revenus de 2007 de FHIW et de FHIS et ait questionné Fairmont au sujet de ces déclarations.

[7] Les intimées veulent maintenant soustraire Fairmont à cette obligation en priant la Cour de rectifier les résolutions adoptées en 2007 par les administrateurs de FHIW et de FHIS. Plus précisément, elles désirent convertir le rachat des actions par Fairmont en un prêt au moyen duquel FHIW et FHIS prêteront à Fairmont la même somme qu'elles lui ont versée pour le rachat des actions.

B. *Historique judiciaire*

(1) Cour supérieure de justice — Le juge Newbould (2014 ONSC 7302, 123 O.R. (3d) 241)

[8] S'appuyant sur l'arrêt *Juliar c. Canada (Attorney General)* (1999), 46 O.R. (3d) 104 (C.S.J.), conf. par (2000), 50 O.R. (3d) 728 (C.A.), de la Cour d'appel de l'Ontario, le juge siégeant en cabinet a accueilli la demande de rectification. Il a conclu que, depuis 2002, Fairmont souhaitait que son entente de financement avec Legacy atteigne la neutralité fiscale et que cette intention a subsisté après l'acquisition de Fairmont en 2006 par Kingdom Hotels et Colony Capital (par. 32).

[9] The chambers judge also found that, in light of the foreign exchange tax exposure presented to Fairmont's subsidiaries by that acquisition, Fairmont intended "at some point in the future" to address "the unhedged position of [FHIW] and [FHIS] in a way that would be tax . . . neutral although they had no specific plan as to how they would do that" (para. 33). Observing (at para. 42) that the tax liability arose as a result of inadvertence by a member of Fairmont's senior management team, he said that this was not "a case in which tax planning has been done on a retroactive basis after a CRA audit", but rather a case in which a "redemption of the preference shares was mistakenly chosen as the means" to "unwind the loans on a tax-free basis" (para. 43). "[D]enial of the application to rectify would", he concluded, "result in a tax burden which Fairmont sought to avoid from the inception of the 2002 reciprocal loan arrangement" while "giv[ing] CRA an unintended gain" (para. 44). And, in any event, he noted that *Juliar* was binding on him in the circumstances (para. 41).

(2) Court of Appeal — Simmons, Cronk and Blair JJ.A. (2015 ONCA 441, 45 B.L.R. (5th) 230)

[10] In brief reasons for judgment, the Court of Appeal affirmed the chambers judge's decision, taking note of his findings regarding Fairmont's continuing intention from 2002 that its financing arrangement with Legacy would be carried out on a tax neutral basis; that this intention subsisted after Fairmont's acquisition in 2006; that the adverse tax consequence was triggered by a mistake in 2007 on the part of a member of Fairmont's senior management; and that the purpose of the 2007 resolutions was not to redeem the shares, but rather "to unwind [the Legacy transactions] on a tax free basis" (para. 7).

[11] The Court of Appeal also commented on the evidentiary burden resting on the party seeking rectification. *Juliar*, it said, "does not require that the

[9] Le juge siégeant en cabinet a également conclu que, comme les filiales de Fairmont s'exposaient à un risque fiscal sur les opérations de change en raison de cette acquisition, Fairmont voulait régler [TRADUCTION] « ultérieurement » le problème de « la position non couverte de [FHIW] et de [FHIS] afin de préserver la neutralité fiscale [. . .], tout en n'ayant aucune idée précise de la façon dont elle s'y prendrait » (par. 33). Faisant observer (par. 42) que l'obligation fiscale a pris naissance à cause de l'inattention d'un membre de la haute direction de Fairmont, le juge siégeant en cabinet a affirmé qu'il ne s'agissait pas d'« un cas où la planification fiscale a été faite rétroactivement après une vérification de l'ARC », mais plutôt d'un cas où le « rachat des actions privilégiées a été choisi par erreur comme moyen » d'« annuler les prêts de façon neutre sur le plan fiscal » (par. 43). Il a conclu que [TRADUCTION] « le rejet de la demande de rectification entraînerait un fardeau fiscal que Fairmont a cherché à éviter depuis la naissance du contrat de prêts réciproques de 2002 » tout en « donn[ant] à l'ARC un gain non intentionnel » (par. 44). Et, quoi qu'il en soit, il a souligné qu'il était lié par l'arrêt *Juliar* dans les circonstances (par. 41).

(2) Cour d'appel — Les juges Simmons, Cronk et Blair (2015 ONCA 441, 45 B.L.R. (5th) 230)

[10] Dans de brefs motifs de jugement, la Cour d'appel a confirmé la décision du juge siégeant en cabinet et a pris note de ses conclusions concernant le fait que l'intention constante de Fairmont, dès 2002, était que son entente de financement avec Legacy soit exécutée de façon neutre sur le plan fiscal, que cette intention a subsisté après l'acquisition de Fairmont en 2006, que la conséquence fiscale négative résulte d'une erreur commise en 2007 par un membre de la haute direction de Fairmont et que l'objectif des résolutions de 2007 n'était pas de racheter les actions, mais plutôt [TRADUCTION] « d'annuler [les opérations de Legacy] de façon neutre sur le plan fiscal » (par. 7).

[11] La Cour d'appel a également formulé des commentaires sur le fardeau de la preuve qui incombe à la partie sollicitant la rectification. Selon

party seeking rectification must have determined the precise mechanics or means by which [its] settled intention to achieve a specific tax outcome would be realized" (para. 10). Rather, "*Juliar* holds, in effect, that the critical requirement for rectification is proof of a continuing specific intention to undertake a transaction or transactions on a particular tax basis" (para. 10). In this case, then, it was in the court's view unnecessary for Fairmont to prove that it had resolved to use "a specific transactional device — loans — to achieve the intended tax result" (para. 12). Rather, the chambers judge's findings regarding Fairmont's intention, coupled with *Juliar*'s direction regarding the prerequisite intention to obtain rectification, were dispositive of the application in the respondents' favour.

III. Analysis

A. *General Principles and Operation of Rectification*

[12] If by mistake a legal instrument does not accord with the true agreement it was intended to record — because a term has been omitted, an unwanted term included, or a term incorrectly expresses the parties' agreement — a court may exercise its equitable jurisdiction to rectify the instrument so as to make it accord with the parties' true agreement. Alternatively put, rectification allows a court to achieve correspondence between the parties' agreement and the substance of a legal instrument intended to record that agreement, when there is a discrepancy between the two. Its purpose is to give effect to the parties' true intentions, rather than to an erroneous transcription of those true intentions (Swan and Adamski, at §8.229).

[13] Because rectification allows courts to rewrite what the parties had originally intended to be the final expression of their agreement, it is "a potent remedy" (*Snell's Equity* (33rd ed. 2015), by J. McGhee, at pp. 417-18). It must, as this Court has repeatedly stated (*Shafron v. KRG Insurance Brokers (Western)*

elle, l'arrêt *Juliar* [TRADUCTION] « n'exige pas que la partie sollicitant la rectification ait déterminé les mécanismes ou les moyens précis par lesquels [son] intention ferme d'obtenir un résultat fiscal précis serait réalisée » (par. 10). En fait, « l'arrêt *Juliar* indique que la condition essentielle de la rectification est la preuve d'une intention constante et précise d'effectuer une ou des opérations sur un fondement fiscal particulier » (par. 10). En l'espèce, la Cour d'appel était donc d'avis qu'il était inutile pour Fairmont de prouver qu'elle était déterminée à se servir d'« un mécanisme opérationnel précis — des prêts — pour atteindre le résultat fiscal voulu » (par. 12). En fait, les conclusions du juge siégeant en cabinet au sujet de l'intention de Fairmont, jumelées à la directive de l'arrêt *Juliar* concernant l'intention préalable pour obtenir une rectification, lui permettaient de trancher la demande en faveur des intimées.

III. Analyse

A. *Principes généraux et application de la rectification*

[12] Si, par erreur, un instrument juridique ne correspond pas à la véritable entente qu'il était censé consigner — parce qu'une modalité a été omise, qu'une modalité non voulue a été incluse ou qu'une modalité exprime incorrectement l'entente des parties — le tribunal peut exercer sa compétence en equity pour rectifier l'instrument de façon à ce qu'il corresponde à la véritable entente entre les parties. Autrement dit, la rectification permet au tribunal d'assurer la correspondance entre l'entente des parties et le contenu d'un instrument juridique visant à consigner cette entente lorsqu'il y a une divergence entre les deux. Elle a pour but de donner effet aux véritables intentions des parties, plutôt qu'à une transcription erronée de ces véritables intentions (Swan et Adamski, §8.229).

[13] Comme la rectification permet aux tribunaux de réécrire ce que les parties voulaient initialement que soit l'expression finale de leur entente, elle constitue [TRADUCTION] « une réparation puissante » (*Snell's Equity* (33e éd. 2015), par J. McGhee, p. 417-418). Comme la Cour l'a maintes fois affirmé

Inc., 2009 SCC 6, [2009] 1 S.C.R. 157, at para. 56, citing *Performance Industries Ltd. v. Sylvan Lake Golf & Tennis Club Ltd.*, 2002 SCC 19, [2002] 1 S.C.R. 678, at para. 31), be used "with great caution", since a "relaxed approach to rectification as a substitute for due diligence at the time a document is signed would undermine the confidence of the commercial world in written contracts": *Performance Industries*, at para. 31. It bears reiterating that rectification is limited solely to cases where a written instrument has incorrectly recorded the parties' antecedent agreement (Swan and Adamski, at §8.229). It is not concerned with mistakes merely in the making of that antecedent agreement: E. Peel, *The Law of Contract* (14th ed. 2015), at para. 8-059; *Mackenzie v. Coulson* (1869), L.R. 8 Eq. 368, at p. 375 ("Courts of Equity do not rectify contracts; they may and do rectify instruments"). In short, rectification is unavailable where the basis for seeking it is that one or both of the parties wish to amend *not the instrument* recording their agreement, but *the agreement itself*. More to the point of this appeal, and as this Court said in *Performance Industries* (at para. 31), "[t]he court's task in a rectification case is . . . to restore the parties to their original bargain, not to rectify a belatedly recognized error of judgment by one party or the other".

(*Shafron c. KRG Insurance Brokers (Western) Inc.*, 2009 CSC 6, [2009] 1 R.C.S. 157, par. 56, citant *Performance Industries Ltd. c. Sylvan Lake Golf & Tennis Club Ltd.*, 2002 CSC 19, [2002] 1 R.C.S. 678, par. 31), elle doit être utilisée « avec grande prudence », puisque « [t]out assouplissement de l'application de la rectification qui en ferait un substitut à l'exercice de diligence raisonnable lors de la signature d'un document aurait pour effet d'ébranler la confiance du monde des affaires à l'égard des contrats écrits » : *Performance Industries*, par. 31. Il convient de réitérer que la rectification se fait uniquement dans les cas où un instrument écrit a consigné incorrectement l'entente antérieure entre les parties (Swan et Adamski, §8.229). La rectification ne vise pas les erreurs commises simplement lors de la formation de cette entente antérieure : E. Peel, *The Law of Contract* (14e éd. 2015), par. 8-059; *Mackenzie c. Coulson* (1869), L.R. 8 Eq. 368, p. 375 ([TRADUCTION] « Les tribunaux d'equity ne rectifient pas les contrats; ils peuvent rectifier et rectifient les instruments »). Bref, la rectification ne peut être accordée lorsqu'elle est fondée sur le désir de l'une des parties ou des deux de modifier *non pas l'instrument* consignant leur entente, mais *l'entente elle-même*. Plus important encore pour le présent pourvoi, et comme la Cour l'a dit dans l'arrêt *Performance Industries* (par. 31), « [l]a tâche des tribunaux dans une affaire de rectification [. . .] consiste à reconstituer le marché original conclu par les parties, et non à rectifier une erreur de jugement qu'une partie aurait reconnue tardivement ».

[14] Beyond these general guides, the nature of the mistake must be accounted for: Swan and Adamski, at §8.233. Two types of error may support a grant of rectification. The first arises when both parties subscribe to an instrument under a *common* mistake that it accurately records the terms of their antecedent agreement. In such a case, an order for rectification is predicated upon the applicant showing that the parties had reached a prior agreement whose terms are definite and ascertainable; that the agreement was still effective when the instrument was executed; that the instrument fails to record accurately that prior agreement; and that, if rectified as proposed, the instrument would carry out the agreement: *Ship M. F. Whalen v. Pointe Anne Quarries Ltd.* (1921), 63

[14] Hormis ces lignes directrices générales, la nature de l'erreur doit être prise en compte : Swan et Adamski, §8.233. Deux sortes d'erreur peuvent donner ouverture à une rectification. La première survient lorsque les deux parties souscrivent à un instrument sur la foi d'une erreur *commune* selon laquelle il consigne correctement les modalités de l'entente antérieure. En pareilles circonstances, une ordonnance de rectification sera rendue si le demandeur démontre que les parties étaient parvenues à une entente antérieure dont les modalités sont déterminées et déterminables, que l'entente était toujours en vigueur lors de la signature de l'instrument, que l'instrument ne consigne pas correctement l'entente antérieure et que s'il est rectifié tel

S.C.R. 109, at p. 126; McInnes, at p. 820; *Snell's Equity*, at p. 424; *Hanbury and Martin Modern Equity* (20th ed. 2015), by J. Glister and J. Lee, at pp. 848-49; *Hart v. Boutilier* (1916), 56 D.L.R. 620 (S.C.C.), at p. 622.

[15] In *Performance Industries* (at para. 31) and again in *Shafron* (at para. 53), this Court affirmed that rectification is also available where the claimed mistake is *unilateral* — either because the instrument formalizes a unilateral act (such as the creation of a trust), or where (as in *Performance Industries* and *Shafron*) the instrument was intended to record an agreement between parties, but one party says that the instrument does not accurately do so, while the other party says it does. In *Performance Industries* (at para. 31), "certain demanding preconditions" were added to rectify a putative unilateral mistake: specifically, that the party resisting rectification knew or ought to have known about the mistake; and that permitting that party to take advantage of the mistake would amount to "fraud or the equivalent of fraud" (para. 38).

B. *Juliar*

[16] As I have recounted, both courts below considered the Court of Appeal's decision in *Juliar*, coupled with the chambers judge's findings, to be dispositive. In my respectful view, however, *Juliar* is irreconcilable with this Court's jurisprudence and with the narrowly confined circumstances to which this Court has restricted the availability of rectification.

[17] In *Juliar*, the parties had, by a written agreement and in the course of the restructuring of a family business, transferred shares to a corporation in exchange for promissory notes for an amount equal to what the parties believed to be the value of the shares. Upon discovering that the promissory notes were worth more than the shares' value (resulting in the taxpaying party being assessed as having received a taxable deemed dividend),

que proposé, l'instrument exécuterait l'entente : *Ship M. F. Whalen c. Pointe Anne Quarries Ltd.* (1921), 63 R.C.S. 109, p. 126; McInnes, p. 820; *Snell's Equity*, p. 424; *Hanbury and Martin Modern Equity* (20e éd. 2015), par J. Glister et J. Lee, p. 848-849; *Hart c. Boutilier* (1916), 56 D.L.R. 620 (C.S.C.), p. 622.

[15] Dans l'arrêt *Performance Industries* (par. 31) et de nouveau dans *Shafron* (par. 53), la Cour a confirmé qu'il peut également y avoir rectification lorsque l'erreur invoquée est *unilatérale* — soit parce que l'instrument officialise un acte unilatéral (comme la création d'une fiducie), soit parce que (comme dans *Performance Industries* et *Shafron*) l'instrument vise à consigner l'entente intervenue entre les parties, mais que l'une d'entre elles dit que l'instrument ne le fait pas correctement, alors que l'autre affirme le contraire. Dans *Performance Industries* (par. 31), la rectification de l'erreur unilatérale putative a été assujettie à « certains préalables rigoureux » : plus précisément, que la partie qui s'oppose à la rectification connaissait ou aurait dû connaître l'existence de l'erreur et que le fait de permettre à cette partie de tirer profit de l'erreur constituerait « une fraude ou l'équivalent d'une fraude » (par. 38).

B. *L'arrêt Juliar*

[16] Comme je l'ai déjà dit, les deux juridictions inférieures ont estimé que l'arrêt *Juliar* de la Cour d'appel, jumelé aux conclusions du juge siégeant en cabinet, permettaient de trancher le pourvoi. À mon humble avis, toutefois, l'arrêt *Juliar* est incompatible avec la jurisprudence de la Cour et les circonstances très restreintes auxquelles la Cour a limité le recours en rectification.

[17] Dans l'affaire *Juliar*, les parties avaient, au moyen d'une entente écrite et dans le cadre de la restructuration d'une entreprise familiale, transféré leurs actions à une autre entreprise en échange de billets à ordre d'un montant égal à la valeur des actions estimée par les parties. Après avoir découvert que la valeur des billets à ordre était supérieure à celle des actions (de sorte que la partie assujettie à l'impôt a fait l'objet d'une cotisation comme si

the parties sought rectification in order to convert what had originally been structured as a shares-for-promissory notes transfer into a shares-for-shares transfer (which would have been tax-deferred). For the Court of Appeal, and citing the decision of *Re Slocock's Will Trusts*, [1979] 1 All E.R. 358 (Ch. D.), Austin J.A. held that the written agreement could be rectified as sought, citing the trial judge's finding that the parties had "a common . . . continuing intention" to transfer shares in a way that would avoid immediate tax liability (para. 19). In order to achieve that objective, Austin J.A. said, the deal "had to be . . . a shares for shares transaction" (para. 25).

[18] This reasoning presents several difficulties. First, as many commentators have observed, it is indisputable that *Juliar* has relaxed the requirements for obtaining rectification, and correspondingly expanded the scope of cases in which rectification may be sought and granted beyond that which the governing principles allow (C. Brown and A. J. Cockfield, "Rectification of Tax Mistakes Versus Retroactive Tax Laws: Reconciling Competing Visions of the Rule of Law" (2013), 61 *Can. Tax J.* 563, at p. 571; N. Brooks and K. Brooks, "The Supreme Court's 2013 Tax Cases: Side-Stepping the Interesting, Important and Difficult Issues" (2015), 68 *S.C.L.R.* (2d) 335, at p. 385; K. Janke-Curliss et al., "Rectification in Tax Law: An Overview of Current Cases", in *Tax Dispute Resolution, Compliance, and Administration in Canada* (2013), 21:1, at pp. 21:8 and 21:9).

[19] I agree with this observation. As I have stressed, rectification is available not to cure a party's error in judgment in entering into a particular agreement, but an error in the recording of that agreement in a legal instrument. Alternatively put, rectification aligns the instrument with what the parties agreed to do, and not what, with the benefit of hindsight, they should have agreed to do. The parties' mistake in *Juliar*, however, was not in the recording of their intended agreement to transfer shares for a promissory note, but in selecting that mechanism instead of

elle avait reçu un dividende réputé imposable), les parties ont sollicité une rectification afin de convertir ce qui avait été initialement structuré comme un transfert d'actions en contrepartie de billets à ordre en un échange d'actions (dont l'imposition aurait été reportée). S'exprimant pour la Cour d'appel, et citant l'arrêt *Re Slocock's Will Trusts*, [1979] 1 All E.R. 358 (Div. chanc.), le juge Austin a conclu que l'entente écrite pouvait être rectifiée telle qu'on l'avait demandé et a cité la conclusion du juge de première instance selon laquelle les parties avaient [TRADUCTION] « une intention commune constante » de transférer les actions de façon à éviter toute obligation fiscale immédiate (par. 19). Le juge Austin a affirmé que pour atteindre cet objectif, il fallait « procéder à un échange d'actions » (par. 25).

[18] Ce raisonnement présente plusieurs difficultés. Premièrement, comme bon nombre de commentateurs l'ont fait remarquer, il est indéniable que l'arrêt *Juliar* a assoupli les exigences à respecter pour obtenir une rectification, et qu'il a élargi en conséquence la portée des cas où la rectification peut être sollicitée et accordée au-delà de celle permise par les principes applicables (C. Brown et A. J. Cockfield, « Rectification of Tax Mistakes Versus Retroactive Tax Laws : Reconciling Competing Visions of the Rule of Law » (2013), 61 *Rev. fisc. can.* 563, p. 571; N. Brooks et K. Brooks, « The Supreme Court's 2013 Tax Cases : Side-Stepping the Interesting, Important and Difficult Issues » (2015), 68 *S.C.L.R.* (2d) 335, p. 385; K. Janke-Curliss et autres, « Rectification in Tax Law : An Overview of Current Cases », dans *Tax Dispute Resolution, Compliance, and Administration in Canada* (2013), 21:1, p. 21:8 et 21:9).

[19] Je souscris à cette observation. Comme je l'ai souligné, il est possible de recourir à la rectification pour corriger non pas une erreur de jugement commise par une partie dans la conclusion d'une entente en particulier, mais une erreur dans la consignation de cette entente dans un instrument juridique. Autrement dit, la rectification fait correspondre l'instrument avec ce que les parties ont convenu de faire, et non avec, en rétrospective, ce qu'elles auraient dû convenir de faire. Dans l'affaire *Juliar*, toutefois, l'erreur des parties ne résidait

a shares-for-shares transfer. By granting the sought-after change of mechanism, the Court of Appeal in *Juliar* purported to "rectify" not merely the instrument recording the parties' antecedent agreement, but that agreement itself where it failed to achieve the desired result or produced an unanticipated adverse consequence — that is, where it was the product of an error in judgment. As J. Berryman observed (in *The Law of Equitable Remedies* (2nd ed. 2013), at p. 510):

In *Juliar*, the applicants had acted directly on the advice of their accountant. The accountant made a mistake as to the nature of the business ownership and the taxes that were paid prior to the arrangement he advised his clients to pursue. This is not a case for rectification. The clients intended to use the instrument given to them by their accountant. Their motive may have been to avoid tax but that is different from their intent which was to use the very form in front of them.

[20] Secondly, even on its own terms, *Juliar*'s expansion of the availability of rectification cannot be justified. By way of explanation, in the case upon which Austin J.A. relied, *Re Slocock's Will Trusts*, the plaintiff was the life beneficiary of her father's residuary estate, with the capital and income after her death to be paid to her issue as she should appoint. She appointed her children to take after her death. Later, lands owned by her father's family were sold to a development company, with the proceeds to be received and distributed by a management company in which the plaintiff received an allotment of shares, proportionate to her interest in the proceeds. After taking legal advice, the plaintiff and her children decided that she should surrender by deed her life interest in those proceeds as well as her shares in the management company (pp. 359-60). The deed, however, did not faithfully record the parties' agreement, because it released only the plaintiff's shares in the management company, and

pas dans la consignation de l'entente dont elles avaient convenu, soit de transférer des actions en contrepartie d'un billet à ordre, mais plutôt dans le fait d'avoir choisi ce mécanisme au lieu d'un échange d'actions. En accordant le changement de mécanisme sollicité après coup, la Cour d'appel a, dans *Juliar*, voulu « rectifier » non seulement l'instrument consignant l'entente antérieure des parties, mais l'entente elle-même, dans la mesure où elle ne permettait pas d'atteindre le résultat voulu, ou entraînait une conséquence fâcheuse imprévue — c'est-à-dire, dans la mesure où elle résultait d'une erreur de jugement. Comme l'a fait remarquer J. Berryman (dans *The Law of Equitable Remedies* (2e éd. 2013), p. 510) :

[TRADUCTION] Dans *Juliar*, les demandeurs avaient agi directement sur le conseil de leur comptable. Le comptable s'est mépris sur la nature du capital-actions de l'entreprise et sur l'impôt qui avait été payé avant la formation de l'entente qu'il avait conseillé à ses clients de conclure. Il n'y a pas lieu d'accorder la rectification en l'espèce. Les clients entendaient utiliser le document que leur comptable leur avait remis. Leur motivation était peut-être d'éviter de payer de l'impôt, mais celle-ci est différente de leur intention, qui était d'utiliser le formulaire dont ils disposaient.

[20] Deuxièmement, même si l'on tient compte des énoncés de l'arrêt *Juliar* comme tels, cet arrêt élargit le recours en rectification d'une façon qui ne saurait être justifiée. En effet, dans l'affaire sur laquelle s'est fondé le juge Austin, *Re Slocock's Will Trusts*, la demanderesse était bénéficiaire d'un intérêt viager sur le reliquat de la succession de son père, dont le capital et le revenu devaient être transmis, après le décès de la demanderesse, aux descendants qu'elle désignerait. Elle a désigné ses enfants. Plus tard, les terres appartenant à la famille de son père ont été vendues à une société de développement, et le produit de la vente a été versé à une société de gestion et réparti par celle-ci. La société de gestion a émis au nom de la demanderesse des actions en proportion de son intérêt dans le produit. Après avoir discuté avec un conseiller juridique, la demanderesse et ses enfants ont décidé qu'elle devrait céder par acte sa participation viagère dans ce produit ainsi que ses actions dans la société de

not her beneficial interest in the proceeds of sale (p. 360).

[21] While the outcome sought by the plaintiff and her children would have also secured a tax advantage for the children (specifically, avoidance of capital transfer tax upon the plaintiff's death), Graham J. granted rectification *not* to secure that tax advantage, but on the strength of his finding (*Re Slocock's Will Trusts*, at p. 361) that the deed as recorded omitted the proceeds of the sale of the lands, thereby failing to record fully the terms of the parties' original agreement. This was, therefore, an unremarkable application of rectification to cure an omission in the instrument recording an antecedent agreement. Nothing in *Re Slocock's Will Trusts* justifies *Juliar*'s modified threshold for granting rectification solely to avoid an unanticipated tax liability. *Re Slocock's Will Trusts* simply confirmed that, provided that the underlying mechanism by which the parties had agreed to seek a particular tax outcome was omitted or incorrectly recorded, and provided that all other conditions for granting rectification are satisfied, a court retains discretion to grant rectification. The focus of the inquiry remained properly fixed on whether that originally intended mechanism was properly recorded, and not on whether it achieved the desired tax outcome or resulted in a party incurring an undesired or unexpected tax outcome.

[22] Subsequent English authorities confirm that *Re Slocock's Will Trusts* created no distinct threshold for granting rectification in the tax context. In *Racal Group Services Ltd. v. Ashmore* (1995), 68 T.C. 86 (C.A.), the English Court of Appeal made clear that a mere intention to obtain a fiscal objective is insufficient to ground a claim in rectification: ". . . the court cannot rectify a document merely on the ground that it failed to achieve the grantor's fiscal objective. The

gestion (p. 359-360). Toutefois, l'acte ne consignait pas fidèlement l'entente des parties, car il ne prévoyait que la renonciation de la demanderesse à ses actions dans la société de gestion, et non la renonciation à son intérêt bénéficiaire dans le produit de la vente (p. 360).

[21] Bien que le résultat recherché par la demanderesse et ses enfants aurait également assuré un avantage fiscal aux enfants (plus précisément, éviter de payer des droits de cession au décès de la demanderesse), le juge Graham a accordé la rectification *non pas* pour assurer cet avantage fiscal, mais sur la foi de sa conclusion (*Re Slocock's Will Trusts*, p. 361) selon laquelle l'acte tel que rédigé passait sous silence le produit de la vente des terres, et ne consignait donc pas entièrement les modalités de l'entente initiale entre les parties. Par conséquent, le juge a appliqué la doctrine de la rectification dans son sens ordinaire pour corriger une omission dans l'instrument consignant l'entente antérieure. Rien dans l'arrêt *Re Slocock's Will Trusts* ne justifie le seuil modifié dans l'arrêt *Juliar* pour accorder une rectification uniquement dans le but d'éviter une obligation fiscale imprévue. L'arrêt *Re Slocock's Will Trusts* a simplement confirmé que, pourvu que le mécanisme sous-jacent au moyen duquel les parties avaient convenu de produire un résultat fiscal en particulier ait été omis ou consigné incorrectement, et pourvu que toutes les autres conditions d'octroi d'une rectification soient réunies, le tribunal conserve le pouvoir discrétionnaire d'accorder la rectification. L'examen est demeuré axé à bon droit sur la question de savoir si ce mécanisme dont les parties avaient convenu au départ était adéquatement constaté, et non sur la question de savoir s'il avait atteint le résultat fiscal désiré ou s'il avait produit un résultat fiscal non désiré ou imprévu pour une partie.

[22] Des décisions anglaises subséquentes confirment que l'arrêt *Re Slocock's Will Trusts* n'a établi aucun critère distinct permettant d'accorder la rectification dans le contexte fiscal. Dans *Racal Group Services Ltd. c. Ashmore* (1995), 68 T.C. 86 (C.A.), la Cour d'appel d'Angleterre a indiqué clairement que la simple intention d'atteindre un objectif fiscal est insuffisante pour fonder une demande de rectification : [TRADUCTION] « . . . le tribunal ne peut

specific intention of the grantor as to how the objective was to be achieved must be shown if the court is to order rectification" (p. 106). Similarly, the court in *Ashcroft v. Barnsdale*, [2010] EWHC 1948, [2010] S.T.C. 2544 (Ch. D.), held that it could not rectify an instrument "*merely* because it fails to achieve the fiscal objectives of the parties to it": para. 17 (emphasis in original). See also D. Hodge, *Rectification: The Modern Law and Practice Governing Claims for Rectification for Mistake* (2nd ed. 2016), at para. 4-145:

> A mere misapprehension as to the tax consequences of executing a particular document will not justify an order for its rectification. The specific intention of the parties (or the grantor or covenantor) as to how the objective was to be achieved must be shown if the court is to order rectification. [Emphasis deleted.]

[23] Finally, *Juliar* does not account for this Court's direction, in *Shell Canada Ltd. v. Canada*, [1999] 3 S.C.R. 622, at para. 45, that a taxpayer should expect to be taxed "based on what it actually did, not based on what it could have done". While this statement in *Shell Canada* was applied to support the proposition that a taxpayer should not be denied a sought-after fiscal objective merely because others had not availed themselves of the same advantage, it cuts the other way, too: taxpayers should not be judicially accorded a benefit based solely on what they would have done had they known better.

[24] This point goes to the respondents' submission that "[r]ectification is necessary to . . . avoid unjust enrichment of the Crown" (R.F., at para. 76), echoing the Court of Appeal's concern in *Juliar* (at paras. 33-34, quoting *Re Slocock's Will Trusts*, at p. 363) for the Crown's "accidental and unexpected windfall" and the chambers judge's concern in the present appeal (at para. 44) about the CRA's "unintended gain" and (at para. 52) the Crown's "tax windfall". With respect, the premise underlying

rectifier un document simplement au motif qu'il n'a pas atteint l'objectif fiscal du concédant. L'intention précise du concédant quant à la façon dont l'objectif devait être atteint doit être démontrée pour que le tribunal ordonne la rectification » (p. 106). De même, le tribunal dans *Ashcroft c. Barnsdale*, [2010] EWHC 1948, [2010] S.T.C. 2544 (Div. chanc.), a conclu qu'il ne pouvait rectifier un instrument [TRADUCTION] « *simplement* parce qu'il n'atteint pas les objectifs fiscaux des parties » : par. 17 (en italique dans l'original). Voir aussi D. Hodge, *Rectification : The Modern Law and Practice Governing Claims for Rectification for Mistake* (2e éd. 2016), par. 4-145 :

> [TRADUCTION] Une simple erreur quant aux conséquences fiscales de la signature d'un document donné ne justifiera pas une ordonnance visant sa rectification. L'intention précise des parties (ou du concédant ou du covenantant) quant à la façon dont l'objectif devait être atteint doit être démontrée pour que le tribunal ordonne la rectification. [Italiques omis.]

[23] Enfin, l'arrêt *Juliar* ne tient pas compte de la directive donnée par la Cour dans *Shell Canada Ltée c. Canada*, [1999] 3 R.C.S. 622, par. 45, selon laquelle un contribuable devrait s'attendre à être imposé « en fonction de ce qu'il a fait, et non de ce qu'il aurait pu faire ». Bien que cet énoncé dans *Shell Canada* ait été appliqué à l'appui de la proposition qu'un contribuable ne devrait pas se voir refuser un objectif fiscal sollicité après coup simplement parce que d'autres ne se sont pas prévalus du même avantage, il joue également dans l'autre sens : les contribuables ne devraient pas se voir accorder un avantage par les tribunaux uniquement sur la base de ce qu'ils auraient fait s'ils avaient su.

[24] Cela m'amène à l'argument des intimées selon lequel [TRADUCTION] « [l]a rectification est nécessaire pour [. . .] éviter que la Couronne ne s'enrichisse sans cause » (m.i., par. 76), qui reprend la préoccupation exprimée par la Cour d'appel dans *Juliar* (par. 33-34, citant *Re Slocock's Will Trusts*, p. 363) à l'égard du [TRADUCTION] « gain accidentel et inattendu » de la Couronne et la préoccupation du juge siégeant en cabinet dans la présente affaire (par. 44) au sujet du « gain non intentionnel » de

such concerns misses the point of the inquiry, inasmuch as it concerns the CRA. Tax consequences, including those which follow an assessment by the CRA, flow from freely chosen legal arrangements, not from the intended or unintended effects of those arrangements, whether upon the taxpayer or upon the public treasury. The proper inquiry is no more into the "windfall" for the public treasury when a taxpayer loses a benefit than it is into the "windfall" for the taxpayer when that taxpayer secures a benefit. The inquiry, rather, is into what the taxpayer agreed to do. *Juliar* erroneously departed from this principle, and in so doing allowed for impermissible retroactive tax planning: *Harvest Operations Corp. v. Canada (Attorney General)*, 2015 ABQB 327, [2015] 6 C.T.C. 78, at para. 49.

C. *Two Further Concerns*

[25] Before applying the test for rectification — which test, I emphasize, is to be applied in a tax context just as it is in a non-tax context — to the facts of this appeal, I turn to two matters in need of clarification, the first of which was raised by the respondents.

(1) "Common Continuing Intention" to Avoid Tax Liability

[26] The respondents argue that, in the case of a common mistake, it is unnecessary for the party seeking rectification to prove a prior agreement concerning the term or terms for which rectification is sought. Rather, they say that evidence of a "common continuing intention" — in this case, their common continuing intention that the value of the shares in FHIW and FHIS should be transferred in a way that would avoid immediate tax liability — should suffice to ground a grant of rectification.

l'ARC et (par. 52) du « gain fiscal fortuit » de la Couronne. Soit dit en tout respect, la prémisse de ces préoccupations n'a rien à voir avec la question qui nous occupe, dans la mesure où elle concerne l'ARC. Les conséquences fiscales, y compris celles qui font suite à une cotisation de l'ARC, découlent directement d'ententes juridiques librement choisies, et non des effets recherchés ou non recherchés de ces ententes, peu importe que ce soit le contribuable ou le trésor public qui les subissent. La question qui se pose en l'espèce ne concerne pas plus le « gain fortuit » du trésor public lorsqu'un contribuable perd un avantage qu'elle ne concerne le « gain fortuit » du contribuable lorsqu'il obtient un avantage. Il s'agit plutôt de savoir ce que le contribuable a convenu de faire. L'arrêt *Juliar* s'est écarté à tort de ce principe et, ce faisant, il a autorisé une planification fiscale rétroactive inadmissible : *Harvest Operations Corp. c. Canada (Attorney General)*, 2015 ABQB 327, [2015] 6 C.T.C. 78, par. 49.

C. *Deux autres préoccupations*

[25] Avant d'appliquer le critère de rectification — critère qui, je le souligne, doit être appliqué dans un contexte fiscal exactement de la même manière que dans un contexte non fiscal — aux faits du présent pourvoi, je me pencherai sur deux questions qui nécessitent des précisions, dont la première a été soulevée par les intimées.

(1) L'« intention commune constante » d'éviter une obligation fiscale

[26] Les intimées font valoir que, dans le cas d'une erreur commune, il n'est pas nécessaire pour la partie qui sollicite la rectification de prouver l'existence d'une entente antérieure relative à la ou aux modalités dont la rectification est demandée. Elles affirment plutôt que la preuve d'une [TRADUCTION] « intention commune constante » — en l'espèce, leur intention commune constante que la valeur des actions dans FHIW et FHIS devrait être transférée d'une façon qui permettrait d'échapper à une obligation fiscale immédiate — devrait suffire à accorder une rectification.

[27] This was, of course, the view of the Court of Appeal, both in *Juliar* and in the present appeal. The respondents also rely upon the decision of the English Court of Appeal in *Joscelyne v. Nissen*, [1970] 2 Q.B. 86, in which the court (at p. 95) approved of this statement of Simonds J. in *Crane v. Hegeman-Harris Co.*, [1939] 1 All E.R. 662:

> . . . in order that this court may exercise its jurisdiction to rectify a written instrument, it is not necessary to find a concluded and binding contract between the parties antecedent to the agreement which it is sought to rectify. . . . [I]t is sufficient to find a common continuing intention in regard to a particular provision or aspect of the agreement. If one finds that, in regard to a particular point, the parties were in agreement up to the moment when they executed their formal instrument, and the formal instrument does not conform with that common agreement, then this court has jurisdiction to rectify, although it may be that there was, until the formal instrument was executed, no concluded and binding contract between the parties. [p. 664]

[28] *Joscelyne*'s statement on the sufficiency of a common continuing intention has been adopted by the Ontario Court of Appeal in *Wasauksing First Nation v. Wasausink Lands Inc.* (2004), 184 O.A.C. 84, at para. 77, and the Newfoundland and Labrador Supreme Court in *Dynamex Canada Inc. v. Miller* (1998), 161 Nfld. & P.E.I.R. 97 (C.A.), at paras. 23 and 27. It is not immediately apparent, however, that it supports the respondents' position here. *Joscelyne*'s reference to "a common continuing intention in regard to a particular provision or aspect of the agreement", coupled with its reference to the later discovery that "the formal instrument does not conform with that common agreement", strongly suggests that — howsoever often *Joscelyne* has been taken as suggesting otherwise by Canadian courts — it does not posit that, in the case of a common mistake, anything less than a prior *agreement* with respect to the term to be rectified is sufficient to support a grant of rectification. While *Joscelyne* allows for situations in which a contract will be unenforceable until a corresponding written instrument is executed (for example, in the case of a transfer of an interest in realty) and for situations

[27] Évidemment, ce point de vue était aussi celui de la Cour d'appel, tant dans l'arrêt *Juliar* que dans le présent pourvoi. Les intimées se sont également appuyées sur l'arrêt *Joscelyne c. Nissen*, [1970] 2 Q.B. 86, dans lequel la Cour d'appel d'Angleterre (p. 95) a approuvé l'affirmation suivante du juge Simonds dans *Crane c. Hegeman-Harris Co.*, [1939] 1 All E.R. 662 :

> [TRADUCTION] . . . pour que le tribunal puisse exercer son pouvoir de rectifier un instrument écrit, il n'est pas nécessaire de conclure à l'existence d'un contrat conclu et exécutoire entre les parties qui précède l'entente dont la rectification est sollicitée. [. . .] [I]l suffit de conclure à l'existence d'une intention commune constante à l'égard d'une clause ou d'un aspect précis de l'entente. Si l'on conclut, à l'égard d'un point en particulier, que les parties étaient d'accord jusqu'au moment où elles ont signé leur instrument officiel, et que cet instrument officiel ne correspond pas à cette entente commune, notre cour a compétence pour accorder la rectification, bien qu'il se peuve qu'avant la signature de l'instrument officiel, aucun contrat exécutoire entre les parties n'ait été conclu. [p. 664]

[28] L'affirmation de l'arrêt *Joscelyne* sur le caractère suffisant d'une intention commune constante a été adoptée par la Cour d'appel de l'Ontario dans *Wasauksing First Nation c. Wasausink Lands Inc.* (2004), 184 O.A.C. 84, par. 77, et par la Cour suprême de Terre-Neuve-et-Labrador dans *Dynamex Canada Inc. c. Miller* (1998), 161 Nfld. & P.E.I.R. 97 (C.A.), par. 23 et 27. Toutefois, il n'est pas évident à première vue que cette affirmation étaye la thèse des intimées en l'espèce. Dans *Joscelyne*, la cour parle d'une [TRADUCTION] « intention commune constante à l'égard d'une clause ou d'un aspect précis de l'entente », et de la découverte après coup que « l'instrument officiel ne correspond pas à cette entente commune », ce qui donne fortement à penser que — peu importe le nombre de fois où l'arrêt *Joscelyne* a été considéré comme suggérant le contraire par les tribunaux canadiens — cet arrêt n'établit pas que, dans le cas d'une erreur commune, quelque chose de moins qu'une *entente* antérieure à propos de la modalité à rectifier suffit pour accorder une rectification. Bien que l'arrêt *Joscelyne* ouvre la porte aux situations où un contrat ne sera pas exécutoire avant la signature d'un instrument écrit correspondant (par

in which there may not have been agreement on all essential terms before the written instrument was executed, this does not detract from its implicit affirmation that rectification requires the parties to show an antecedent agreement with respect to the term or terms for which rectification is sought.

[29] In any event, *Joscelyne* should not be taken as authorizing any departure from this Court's direction that a party seeking to correct an erroneously drafted written instrument on the basis of a common mistake must first demonstrate its inconsistency with an antecedent agreement with respect to that term. In *Shafron*, this Court unambiguously rejected the sufficiency of showing mere *intentions* to ground a grant of rectification, insisting instead on erroneously recorded *terms*. As Denning L.J. said in *Frederick E. Rose (London) Ld. v. William H. Pim Jnr. & Co.*, [1953] 2 Q.B. 450 (C.A.), at p. 461 (quoted in *Shafron*, at para. 52):

> Rectification is concerned with contracts and documents, not with intentions. In order to get rectification it is necessary to show that the parties were in complete agreement on the terms of their contract, but by an error wrote them down wrongly; and in this regard, in order to ascertain the terms of their contract, you do not look into the inner minds of the parties — into their intentions — any more than you do in the formation of any other contract.

[30] This Court's statement in *Performance Industries* (at para. 31) that "[r]ectification is predicated on the existence of a prior oral contract whose terms are definite and ascertainable" is to the same effect. The point, again, is that rectification corrects the recording in an instrument of an agreement (here, to redeem shares). Rectification does not operate simply because an agreement failed to achieve an intended effect (here, tax neutrality) — irrespective of whether the intention to achieve that effect was "common" and "continuing".

exemple, dans le cas du transfert d'un intérêt dans un bien immobilier) et à celles où les parties ne se sont peut-être pas entendues sur toutes les conditions essentielles avant la signature de l'instrument écrit, cela ne diminue en rien son affirmation implicite selon laquelle la rectification nécessite que les parties démontrent l'existence d'une entente antérieure à propos de la ou des modalités dont la rectification est demandée.

[29] Quoi qu'il en soit, on ne doit pas considérer que l'arrêt *Joscelyne* autorise tout écart par rapport à la directive de la Cour selon laquelle la partie qui cherche à corriger un instrument écrit erronément rédigé sur le fondement d'une erreur commune doit d'abord démontrer qu'il ne correspond pas à une entente antérieure au sujet de la modalité en cause. Dans *Shafron*, la Cour a rejeté sans équivoque l'idée qu'il suffit de démontrer de simples *intentions* pour fonder une rectification, insistant plutôt sur des *modalités* mal consignées. Comme le juge Denning l'a affirmé dans *Frederick E. Rose (London) Ld. c. William H. Pim Jnr. & Co.*, [1953] 2 Q.B. 450 (C.A.), p. 461 (cité dans *Shafron*, par. 52) :

> [TRADUCTION] La rectification concerne les contrats et les documents, et non les intentions. Pour obtenir une rectification, il faut démontrer que les parties étaient parfaitement d'accord sur les stipulations du contrat, mais qu'elles ont fait une erreur lorsqu'elles les ont consignées par écrit; et il n'y a pas davantage lieu à cet égard, pour établir les conditions du contrat conclu, de sonder la pensée des parties — de sonder leurs intentions — qu'il n'y a lieu de le faire à propos de la formation de tout autre contrat.

[30] L'affirmation de la Cour dans l'arrêt *Performance Industries* (par. 31) selon laquelle « [l]a rectification est fondée sur l'existence d'un contrat verbal préalable dont les conditions sont déterminées et déterminables » va dans le même sens. Encore une fois, le fait est que la rectification corrige la consignation d'une entente (visant en l'espèce à racheter des actions) dans un instrument. La rectification ne se fait pas simplement parce qu'une entente n'a pas produit l'effet voulu (en l'espèce, la neutralité fiscale) — peu importe si l'intention d'obtenir cet effet était « commune » et « constante ».

[31] In this regard, my colleague Justice Abella relies upon the chambers judge's finding that "when the 2006 transaction was undertaken, Fairmont had an intent that at some point in the future [it] would have to deal with the unhedged position of [FHIW and FHIS] in a way that would be tax and accounting neutral although [it] had no specific plan as to how [it] would do that" (para. 33, cited by Abella J. at para. 87). In my respectful view, however, it was an error for the chambers judge to ascribe any significance to that finding. Rectification does not correct common mistakes in judgment that frustrate contracting parties' aspirations or, as here, unspecified "plans"; it corrects common mistakes in instruments recording the terms by which parties, wisely or unwisely, agreed to pursue those aspirations. While my colleague suggests that the jurisprudence of this Court undermines this reasoning (paras. 79-85), that very jurisprudence requires the party seeking rectification of an instrument to show not merely an inchoate or otherwise undeveloped "intent", but rather the term of an antecedent *agreement* which was not correctly recorded therein: *Performance Industries*, at para. 37.

[31] À cet égard, ma collègue la juge Abella s'appuie sur la conclusion du juge siégeant en cabinet [TRADUCTION] « qu'en 2006, au moment de procéder à l'opération, Fairmont entendait régler ultérieurement le problème de la position non couverte de [FHIW et de FHIS] sans incidences fiscales ou comptables, tout en n'ayant aucune idée précise de la façon dont elle s'y prendrait » (par. 33, cité par la juge Abella au par. 87). Avec égards toutefois, je suis d'avis que le juge siégeant en cabinet a eu tort d'accorder quelque importance que ce soit à cette conclusion. La rectification ne corrige ni les erreurs de jugement communes qui vont à l'encontre des aspirations des parties contractantes, ni, comme en l'espèce, des « idées » imprécises; elle corrige les erreurs communes commises dans les instruments qui consignent les modalités auxquelles les parties ont convenu, judicieusement ou imprudemment, de poursuivre ces aspirations. Bien que ma collègue laisse entendre que la jurisprudence de la Cour affaiblit ce raisonnement (par. 79-85), cette même jurisprudence oblige la partie sollicitant la rectification d'un instrument à démontrer non pas une « intention » vague ou par ailleurs mal définie, mais la modalité d'une *entente* préalable qui n'a pas été correctement consignée dans cet instrument : *Performance Industries*, par. 37.

[32] It therefore falls to a party seeking rectification to show not only the putative error in the instrument, but also the way in which the instrument should be rectified in order to correctly record what the parties intended to do. "The court's task in a rectification case is corrective, not speculative": *Performance Industries*, at para. 31. Where, therefore, an instrument recording an agreed-upon course of action is sought to be rectified, the party seeking rectification must identify terms which were omitted or recorded incorrectly and which, correctly recorded, are sufficiently precise to constitute the terms of an enforceable agreement. The inclusion of imprecise terms in an instrument is, on its own, not enough to obtain rectification; absent evidence of what the parties had specifically agreed to do, rectification is not available. While imprecision may justify setting aside an instrument, it cannot invite courts to find an agreement where none is present. It was for this reason that the Court in

[32] Il incombe donc à la partie qui sollicite la rectification de démontrer non seulement l'erreur putative dans l'instrument, mais également la façon dont l'instrument devrait être rectifié afin de consigner correctement ce que les parties avaient l'intention de faire. « La tâche des tribunaux dans une affaire de rectification est de corriger et non de faire des supputations » : *Performance Industries*, par. 31. Par conséquent, lorsqu'une partie cherche à rectifier un instrument consignant une mesure convenue, elle doit indiquer les modalités qui ont été omises ou consignées incorrectement et qui, si elles étaient correctement consignées, seraient suffisamment précises pour constituer les modalités d'une entente exécutoire. L'inclusion de modalités imprécises dans un instrument n'est pas, à elle seule, suffisante pour obtenir une rectification; sans preuve de ce que les parties avaient précisément convenu de faire, il n'est pas possible de recourir à la rectification. Bien qu'une imprécision puisse

Shafron declined to enforce the restrictive covenant covering the "Metropolitan City of Vancouver". The term was imprecise, but there was "no indication that the parties agreed on something and then mistakenly included something else in the written contract": *Shafron*, at para. 57.

[33] As is apparent from the reasons of my colleague Justice Wagner in *Jean Coutu Group (PJC) Inc. v. Canada (Attorney General)*, 2016 SCC 55, [2016] 2 S.C.R. 670, on this question both equity and the civil law are *ad idem*, despite each legal system arriving at that same conclusion via different paths — the former being concerned with correcting the document, and the latter focusing on its interpretation. This convergence is undoubtedly desirable in the context of applying federal tax legislation. More particularly, the cautionary note struck by the Court in *Quebec (Agence du revenu) v. Services Environnementaux AES inc.*, 2013 SCC 65, [2013] 3 S.C.R. 838, at para. 54, regarding "common intention" as a factor in rewriting parties' agreements under art. 1425 of the *Civil Code of Québec* — which precaution is expressly relied upon by Wagner J. in *Jean Coutu* (at para. 21) — is equally apposite in applying the equitable doctrine of rectification:

> Taxpayers should not view this . . . as an invitation to engage in bold tax planning on the assumption that it will always be possible for them to redo their contracts retroactively should that planning fail. A taxpayer's intention to reduce his or her tax liability would not on its own constitute the object of an obligation within the meaning of art. 1373 *C.C.Q.*, since it would not be sufficiently determinate or determinable. Nor would it even constitute the object of a contract within the meaning of art. 1412 *C.C.Q.* Absent a more precise and more clearly defined object, no contract would be formed. In such a case, art. 1425 could not be relied on to justify seeking the common intention of the parties in order to give effect to that intention despite the words of the writings prepared to record it.

justifier l'annulation d'un instrument, elle ne peut amener les tribunaux à conclure à l'existence d'une entente lorsqu'il n'y en a pas. C'est pour cette raison que la Cour a, dans l'arrêt *Shafron*, refusé d'exécuter la clause restrictive couvrant « l'agglomération de la ville de Vancouver ». L'expression était imprécise, mais « rien ne permet[tait] de croire que les parties auraient convenu d'une chose, puis inscrit par erreur quelque chose d'autre dans le contrat écrit » : *Shafron*, par. 57.

[33] Comme il appert des motifs de mon collègue le juge Wagner dans l'arrêt *Groupe Jean Coutu (PJC) inc. c. Canada (Procureur général)*, 2016 CSC 55, [2016] 2 R.C.S. 670, à cet égard, l'equity et le droit civil vont dans le même sens, malgré le fait que chaque système juridique arrive à une même conclusion par des voies différentes — le premier visant la correction du document, et le dernier étant axé sur son interprétation. Cette convergence est indubitablement souhaitable dans l'application des lois fiscales fédérales. Plus particulièrement, la mise en garde formulée par la Cour dans *Québec (Agence du revenu) c. Services Environnementaux AES inc.*, 2013 CSC 65, [2013] 3 R.C.S. 838, par. 54, concernant l'« intention commune » à titre de facteur pour réécrire les ententes des parties en vertu de l'art. 1425 du *Code civil du Québec* — mise en garde sur laquelle s'est fondé expressément le juge Wagner dans *Jean Coutu* (par. 21) — est tout aussi pertinente dans l'application de la doctrine de la rectification en equity :

> En effet, les contribuables ne devraient pas interpréter [cela] comme une invitation à se lancer dans des planifications fiscales audacieuses, en se disant qu'il leur sera toujours possible de refaire leurs contrats rétroactivement en cas d'échec de ces planifications. L'intention d'un contribuable de réduire ses obligations fiscales ne saurait à elle seule constituer l'objet de l'obligation au sens de l'art. 1373 *C.c.Q.*, compte tenu de son caractère insuffisamment déterminé ou déterminable, ni même l'objet du contrat au sens de l'art. 1412 *C.c.Q.* En l'absence d'un objet plus précis et mieux défini, aucun contrat ne serait formé. L'article 1425 ne pourrait dans un tel cas être invoqué pour justifier la recherche de l'intention commune des parties afin de lui donner effet, malgré les termes des écrits préparés pour la constater.

(2) Standard of Proof

[34] The second point requiring clarification is the standard of proof. In *Performance Industries*, at para. 41, this Court held that a party seeking rectification will have to meet all elements of the test by "convincing proof", which it described as "proof that may fall well short of the criminal standard, but which goes beyond the sort of proof that only reluctantly and with hesitation scrapes over the low end of the civil 'more probable than not' standard". This, as was observed in *Performance Industries*, was a relaxation of the standard from the Court's earlier jurisprudence, in which the criminal standard of proof was applied: see *Ship M. F. Whalen*, at p. 127, and *Hart*, at p. 630, per Duff J.

[35] In light, however, of this Court's more recent statement in *F.H. v. McDougall*, 2008 SCC 53, [2008] 3 S.C.R. 41, at para. 40, that there is "only one civil standard of proof at common law and that is proof on a balance of probabilities", the question obviously arises of whether the Court's description in *Performance Industries* of the standard to which the elements of the test for obtaining rectification must be proven is still applicable.

[36] In my view, the applicable standard of proof to be applied to evidence adduced in support of a grant of rectification is that which *McDougall* identifies as the standard generally applicable to all civil cases: the balance of probabilities. But this merely addresses the standard, and not the quality of evidence by which that standard is to be discharged. As the Court also said in *McDougall* (at para. 46), "evidence must always be sufficiently clear, convincing and cogent". A party seeking rectification faces a difficult task in meeting this standard, because the evidence must satisfy a court that the true substance of its unilateral intention or agreement with another party was not accurately recorded in the instrument to which it nonetheless subscribed. A court will typically require evidence exhibiting a high degree of clarity, persuasiveness and cogency before substituting the terms of a written instrument with those

(2) Norme de preuve

[34] Le deuxième point qui nécessite des précisions est la norme de preuve. Dans l'arrêt *Performance Industries*, par. 41, la Cour a conclu que la partie qui sollicite une rectification devra satisfaire à tous les éléments du critère applicable par une « preuve convaincante », qui est décrite comme « une preuve qui peut être bien inférieure à la norme applicable en matière criminelle, mais qui excède toutefois la preuve qui satisfait péniblement à la norme de la "prépondérance des probabilités" applicable en matière civile ». Comme l'a fait observer la Cour dans *Performance Industries*, il s'agit là d'un assouplissement de la norme établie dans la jurisprudence antérieure de la Cour, où la norme de preuve en matière criminelle a été appliquée : voir *Ship M. F. Whalen*, p. 127; *Hart*, p. 630, le juge Duff.

[35] Cependant, à la lumière de l'énoncé plus récent de la Cour dans l'arrêt *F.H. c. McDougall*, 2008 CSC 53, [2008] 3 R.C.S. 41, par. 40, selon lequel il n'existe, « en common law, qu'une seule norme de preuve en matière civile, celle de la prépondérance des probabilités », il faut évidemment se demander si la description de la norme — selon laquelle les éléments du critère à satisfaire pour obtenir la rectification doivent être prouvés — donnée par la Cour dans *Performance Industries* s'applique toujours.

[36] À mon sens, la norme de preuve applicable à la preuve présentée à l'appui d'une demande de rectification est celle qui est désignée dans l'arrêt *McDougall* comme la norme généralement applicable à toutes les affaires civiles : la prépondérance des probabilités. Or, cela désigne simplement la norme, et non la qualité de la preuve nécessaire pour satisfaire à cette norme. Comme la Cour l'a également dit dans *McDougall* (par. 46), « la preuve doit toujours être claire et convaincante ». Il sera difficile pour la partie qui sollicite la rectification de satisfaire à cette norme, car la preuve doit convaincre le tribunal que la véritable substance de son intention unilatérale ou de son entente avec une autre partie n'a pas été consignée correctement dans l'instrument auquel elle a néanmoins souscrit. Le tribunal exigera généralement une preuve très claire, convaincante et solide avant de

said to form the party's true, if only orally expressed, intended course of action. This idea was helpfully encapsulated, in the context of an application for rectification of a common mistake, by Brightman L.J. in *Thomas Bates and Son Ltd. v. Wyndham's (Lingerie) Ltd.*, [1981] 1 W.L.R. 505 (C.A.), at p. 521:

> The standard of proof required in an action of rectification to establish the common intention of the parties is, in my view, the civil standard of balance of probability. But as the alleged common intention ex hypothesi contradicts the written instrument, convincing proof is required in order to counteract the cogent evidence of the parties' intention displayed by the instrument itself. It is not, I think, the standard of proof which is high, so differing from the normal civil standard, but the evidential requirement needed to counteract the inherent probability that the written instrument truly represents the parties' intention because it is a document signed by the parties.

[37] In brief, while the standard of proof is the balance of probabilities, the essential concern of *Performance Industries* remains applicable, being (at para. 42) "to promote the utility of written agreements by closing the 'floodgate' against marginal cases that dilute what are rightly seen to be demanding preconditions to rectification".

D. *Application to the Present Appeal*

[38] To summarize, rectification is an equitable remedy designed to correct errors in the recording of terms in written legal instruments. Where the error is said to result from a mistake common to both or all parties to the agreement, rectification is available upon the court being satisfied that, on a balance of probabilities, there was a prior agreement whose terms are definite and ascertainable; that the agreement was still in effect at the time the instrument was executed; that the instrument fails to accurately record the agreement; and that the instrument, if rectified, would carry out the parties' prior agreement. In the case of a unilateral mistake,

permettre que les modalités d'un instrument écrit soient remplacées par celles qui constateraient la véritable intention des parties, si elle a été exprimée uniquement de vive voix. Cette idée a été utilement résumée dans le contexte d'une demande de rectification d'une erreur commune par le juge Brightman dans l'arrêt *Thomas Bates and Son Ltd. c. Wyndham's (Lingerie) Ltd.*, [1981] 1 W.L.R. 505 (C.A.), p. 521 :

> [TRADUCTION] La norme de preuve à laquelle il faut satisfaire dans une action en rectification pour établir l'intention commune des parties est, à mon sens, la norme civile de la prépondérance des probabilités. Or, puisque l'intention commune présumée contredit l'instrument écrit, une preuve convaincante est nécessaire pour pouvoir contrebalancer la preuve solide de l'intention des parties exprimée par l'instrument lui-même. J'estime qu'il ne s'agit pas d'une norme de preuve élevée, différente de la norme civile ordinaire, mais de l'exigence nécessaire en matière de preuve pour contrebalancer la probabilité inhérente que l'instrument écrit représente véritablement l'intention des parties puisqu'il s'agit d'un document signé par les parties.

[37] En somme, bien que la norme de preuve applicable soit la prépondérance des probabilités, l'objectif essentiel dans l'arrêt *Performance Industries* demeure pertinent, soit (par. 42) « de renforcer l'utilité des ententes écrites en prévenant une "avalanche" d'affaires limites qui affaibliraient des exigences perçues à juste titre comme de rigoureux préalables à la rectification ».

D. *Application au présent pourvoi*

[38] En résumé, la rectification est une réparation en equity visant à corriger les erreurs dans la consignation de modalités dans des instruments juridiques écrits. Lorsqu'on allègue que l'erreur découle d'une erreur commune à toutes les parties à l'entente, le tribunal peut accorder la rectification s'il est convaincu que, selon la prépondérance des probabilités, il y avait une entente antérieure dont les modalités sont déterminées et déterminables, que l'entente était toujours en vigueur au moment de la signature de l'instrument, que l'instrument ne consigne pas correctement l'entente et que l'instrument, s'il est rectifié, exécuterait l'entente

the party seeking rectification must also show that the other party knew or ought to have known about the mistake and that permitting the defendant to take advantage of the erroneously drafted agreement would amount to fraud or the equivalent of fraud.

[39] A straightforward application of these principles to the present appeal leads unavoidably to the conclusion that the respondents' application for rectification should have been dismissed, since they could not show having reached a prior agreement with definite and ascertainable terms. I have already noted (1) the chambers judge's finding that, in 2006, Fairmont intended to address the "unhedged position of [FHIW and FHIS] in a way that would be tax and accounting neutral although [it] had no specific plan as to how [it] would do that" (para. 33); and (2) the Court of Appeal's description of Fairmont's intention as being "to unwind [the Legacy transactions] on a tax free basis" (para. 7). It is therefore clear that Fairmont intended to limit, if not avoid altogether, its tax liability in unwinding the Legacy transactions. And, by redeeming the shares in 2007, this intention was frustrated. Without more, however, these facts do not support a grant of rectification. The error in the courts below is of a piece with the principal flaw I have identified in the Court of Appeal's earlier reasoning in *Juliar*. Rectification is not equity's version of a mulligan. Courts rectify instruments which do not correctly record agreements. Courts do not "rectify" agreements where their faithful recording in an instrument has led to an undesirable or otherwise unexpected outcome.

[40] Relatedly, the respondents do not show how Fairmont's intention, held in common and on a continuing basis with FHIW and FHIS, was to be achieved in definite and ascertainable terms while unwinding the Legacy transactions. The respondents' factum refers to "the original 2006 plan", but that plan was not only imprecise: it really was not a plan at all, being at best an inchoate wish to protect,

antérieure des parties. Dans le cas d'une erreur unilatérale, la partie qui sollicite la rectification doit également démontrer que l'autre partie connaissait ou aurait dû connaître l'existence de l'erreur et que le fait de permettre à l'autre partie de tirer profit de cette entente mal rédigée constituerait une fraude ou l'équivalent d'une fraude.

[39] Une application pure et simple de ces principes au présent pourvoi mène inévitablement à la conclusion que la demande de rectification des intimées aurait dû être rejetée, puisqu'elles n'ont pu démontrer qu'elles avaient conclu une entente antérieure dont les modalités étaient déterminées et déterminables. J'ai déjà souligné (1) la conclusion du juge siégeant en cabinet selon laquelle, en 2006, Fairmont entendait régler le problème de la « position non couverte de [FHIW et de FHIS] sans incidences fiscales et comptables, tout en n'ayant aucune idée précise de la façon dont elle s'y prendrait » (par. 33); (2) la description par la Cour d'appel de l'intention de Fairmont comme étant celle « d'annuler [les opérations de Legacy] de façon neutre sur le plan fiscal » (par. 7). Il est donc clair que Fairmont comptait limiter, voire éviter complètement, son obligation fiscale en annulant les opérations de Legacy. Et le rachat des actions en 2007 a contrecarré cette intention. Sans plus, toutefois, ces faits ne justifient pas l'octroi d'une rectification. L'erreur commise par les juridictions inférieures va de pair avec le vice principal que j'ai relevé dans le raisonnement de la Cour d'appel dans l'arrêt *Juliar*. La rectification n'est pas équivalente en equity à un deuxième essai. Les tribunaux rectifient des instruments qui ne consignent pas correctement une entente. Ils ne « rectifient » pas les ententes dont la consignation fidèle dans un instrument a mené à un résultat indésirable ou par ailleurs imprévu.

[40] Dans le même ordre d'idées, les intimées ne démontrent pas comment l'intention de Fairmont, qu'elle partageait de manière constante avec FHIW et FHIS, devait être réalisée selon des modalités déterminées et déterminables tout en annulant les opérations de Legacy. Le mémoire des intimées renvoie au [TRADUCTION] « plan initial de 2006 », mais ce plan n'était pas seulement imprécis. Il ne

by unspecified means, FHIW and FHIS from foreign exchange tax liability.

[41] The respondents' application for rectification therefore fails at the first hurdle. They show no prior agreement whose terms were definite and ascertainable.

IV. Conclusion and Disposition

[42] I would allow the appeal, with costs in this Court and in the courts below.

The reasons of Abella and Côté JJ. were delivered by

[43] Abella J. (dissenting) — I agree that there is no adjustment to the test for rectification if the context is a tax case. With respect, however, I do not agree that the test was not met in this case.

[44] The doctrine of rectification has many strands. The jurisprudence addresses errors in the transcription and implementation of documents, different types of mistakes, the rights of third parties, and how the remedy applies in various legal contexts. A coherent approach to all of these strands flows from the underlying theory that parties should not be prevented from having their true intentions implemented because of these errors. It is, after all, an equitable remedy that seeks to prevent the unfairness that results from enforcing a mistake, including the unfairness inherent in unjust enrichment and windfalls.

[45] I see the approach applied by my colleague as unduly narrowing its scope. A common, continuing, definite, and ascertainable intention to pursue a transaction in a tax-neutral manner has usually satisfied the threshold for granting rectification. The additional requirement that the parties clearly identify the precise mechanism by which they intended to achieve tax neutrality, and how that mechanism

s'agissait même pas en fait d'un plan. Ce n'était tout au plus qu'un désir incomplet de protéger, par des moyens non précisés, FHIW et FHIS contre une obligation fiscale sur les opérations de change.

[41] La demande de rectification des intimées ne satisfait donc pas à la première exigence. Elles n'ont démontré aucune entente antérieure dont les modalités étaient déterminées et déterminables.

IV. Conclusion et dispositif

[42] Je suis d'avis d'accueillir le pourvoi, avec dépens devant la Cour et les juridictions inférieures.

Version française des motifs des juges Abella et Côté rendus par

[43] La juge Abella (dissidente) — Je conviens qu'il n'y a pas lieu de modifier le test de rectification lorsque l'affaire en cause est de nature fiscale. Avec égards, toutefois, je ne partage pas l'opinion que ce test n'a pas été respecté en l'espèce.

[44] La doctrine de la rectification comporte de multiples facettes. La jurisprudence en la matière traite des erreurs de transcription et d'exécution de documents, de différents types d'erreurs, des droits des tiers et de la façon dont la réparation s'applique dans divers contextes juridiques. L'approche cohérente adoptée à l'égard de toutes ces facettes découle de la théorie sous-jacente qu'on ne devrait pas empêcher les parties de réaliser leurs véritables intentions en raison de telles erreurs. La rectification est, après tout, une réparation en equity visant à prévenir l'injustice qui découle du fait d'avoir donné effet à une erreur, y compris l'injustice inhérente à l'enrichissement injustifié et aux gains fortuits.

[45] J'estime que l'approche adoptée par mon collègue restreint indûment la portée de cette réparation. L'intention commune, constante, déterminée et déterminable de réaliser une opération sans incidences fiscales satisfait habituellement au seuil d'octroi d'une rectification. L'exigence supplémentaire selon laquelle les parties doivent désigner clairement le mécanisme précis au moyen duquel elles ont

was mistakenly transcribed in a document, has the effect of raising the threshold and frustrating the purpose of the remedy. It also has the regrettable effect of imposing a narrower remedy in the common law than exists under civil law.

[46] The Application Judge concluded that the intention of the parties had been mistakenly implemented and that rectification was justified. The Court of Appeal agreed. As do I. Based on the factual findings and the applicable jurisprudence, the threshold has been met. I would dismiss the appeal.

Background

[47] Fairmont Hotels Inc. is a hotel management company. In 2002 and 2003, Fairmont agreed to help Legacy Hotels REIT, a Canadian real estate investment trust in which it owned a minority interest, finance the purchase of two hotels in Washington, D.C. and Seattle, Washington. For tax reasons, Legacy did not directly purchase the hotels. Instead, Legacy and Fairmont created a complex reciprocal loan structure, set up in U.S. dollars, whereby Legacy and Fairmont loaned each other money through their subsidiary corporations. The reciprocal loan structure was designed so that no foreign exchange gains or losses would be realized by Fairmont or its subsidiaries. It was expected to remain in place for 10 years.

[48] In 2006, two companies, Kingdom Hotels International and Colony Capital LLC, purchased Fairmont. Fairmont's tax advisors realized that the change of control would immediately cause Fairmont and its subsidiaries to experience net foreign exchange losses. Fairmont's advisors, in a memo dated March 3, 2006, therefore initially proposed a plan to protect Fairmont and its subsidiaries from those losses. Under this plan, the reciprocal loan structure could later be unwound with a preferred share redemption without triggering any taxable foreign exchange gains. But the tax advisors of Kingdom Hotels and Colony Capital expressed concern that this plan would create other tax problems.

l'intention d'atteindre la neutralité fiscale, ainsi que la manière dont ce mécanisme a été incorrectement transcrit dans le document, a pour effet de hausser le seuil et de contrecarrer l'objet de la réparation. Cette exigence a également l'effet regrettable d'accorder une réparation plus restreinte en common law que celle qui existe en droit civil.

[46] Le juge saisi de la demande a conclu que l'intention des parties avait été mal réalisée et que la rectification était justifiée. La Cour d'appel a souscrit à cette conclusion. Tout comme moi. Compte tenu des conclusions de fait et de la jurisprudence applicable, le seuil a été respecté. Je suis d'avis de rejeter le pourvoi.

Contexte

[47] Hôtels Fairmont Inc. est une société de gestion hôtelière. En 2002 et 2003, Fairmont a consenti à aider Legacy Hotels REIT, une fiducie canadienne d'investissement immobilier dans laquelle elle possédait une participation minoritaire, à financer l'achat de deux hôtels situés à Washington (D.C.) et à Seattle (Washington). Pour des raisons fiscales, Legacy n'a pas acquis directement les hôtels. Legacy et Fairmont ont plutôt élaboré une structure complexe de prêts réciproques, en dollars américains, au moyen de laquelle chacune prêtait de l'argent à l'autre par l'entremise de ses filiales. La structure de prêts réciproques a été conçue pour que Fairmont ou ses filiales ne réalisent aucun gain ou perte sur change. Elle devait rester en place pendant 10 ans.

[48] En 2006, Fairmont a été acquise par deux sociétés, Kingdom Hotels International et Colony Capital LLC. Les conseillers fiscaux de Fairmont se sont rendu compte que le changement de contrôle ferait immédiatement subir à Fairmont et à ses filiales des pertes sur change nettes. Dans une note de service datée du 3 mars 2006, ils ont donc proposé au départ un plan visant à protéger Fairmont et ses filiales de ces pertes. Selon ce plan, la structure de prêts réciproques pourrait être ultérieurement dénouée au moyen d'un rachat d'actions privilégiées, et ce, sans provoquer de gains sur change imposables. Toutefois, les conseillers fiscaux de Kingdom Hotels et de Colony Capital ont dit craindre que ce plan pose d'autres problèmes fiscaux.

[49] Fairmont, Kingdom Hotels, and Colony Capital eventually agreed on a *modified* plan, described in a memo dated March 23, 2006, in which Fairmont would realize certain accrued foreign exchange gains and losses while protecting itself from new gains and losses going forward. This modified plan did not address Fairmont's subsidiaries, which, due to the acquisition, would no longer be protected from foreign exchange exposure. Fairmont was aware that its subsidiaries' exposure would result in a taxable foreign exchange gain if the reciprocal loan structure was later unwound with a share redemption. Since the reciprocal loan structure was to remain in place for several more years, Fairmont decided that, at a later date, it would determine how to unwind the structure without a share redemption so that no accrued gains or losses would be triggered.

[50] In 2007, Legacy asked Fairmont to end the reciprocal loan agreement ahead of schedule so that it could sell the two hotels it had acquired in 2003. Fairmont's Vice-President of Tax, under the mistaken impression that it was the initial March 3, 2006 plan that had been implemented, instructed the directors of Fairmont's subsidiaries to pass resolutions that would unwind the reciprocal loan structure with a share redemption. The directors passed these resolutions implementing the redemption of the preferred shares on September 14, 2007.

[51] The share redemption would have been tax-neutral if the initial plan had in fact been the plan that was implemented. The result of the mistake was to trigger a significantly larger tax liability.

[52] Fairmont learned of this mistake after an audit by the Canada Revenue Agency. It applied to the Ontario Superior Court of Justice to rectify the September 14, 2007 directors' resolutions that had authorized the preferred share redemption. Newbould J. allowed rectification of these resolutions on the grounds that Fairmont never intended to redeem the preferred shares and always intended to unwind the reciprocal loan structure on a tax-neutral basis.

[49] Fairmont, Kingdom Hotels et Colony Capital ont finalement convenu d'un plan *modifié*, décrit dans une note de service datée du 23 mars 2006, selon lequel Fairmont enregistrerait certains gains et pertes sur change accumulés tout en se prémunissant des gains et pertes à venir. Ce plan modifié ne réglait pas la question des filiales de Fairmont qui, en raison de l'acquisition, ne seraient plus protégées contre le risque de change. Fairmont savait que ses filiales risquaient de réaliser un gain sur change imposable si la structure de prêts réciproques devait plus tard être dénouée au moyen d'un rachat d'actions. Puisqu'il était prévu que la structure reste en place pendant encore plusieurs années, Fairmont a décidé qu'elle déterminerait plus tard comment elle la dénouerait sans procéder par rachat d'actions pour éviter de réaliser une perte ou un gain accumulé.

[50] En 2007, Legacy a demandé à Fairmont de mettre fin au contrat de prêts réciproques avant terme de sorte qu'elle puisse vendre les deux hôtels qu'elle avait acquis en 2003. Le vice-président des affaires fiscales de Fairmont, qui croyait à tort que l'on avait mis en œuvre le plan initial du 3 mars 2006, a donné pour instruction aux administrateurs des filiales de Fairmont d'adopter les résolutions nécessaires pour dénouer la structure de prêts réciproques au moyen d'un rachat d'actions. Les administrateurs ont adopté les résolutions mettant en œuvre le rachat des actions privilégiées le 14 septembre 2007.

[51] Le rachat d'actions n'aurait entraîné aucune incidence fiscale si l'on avait effectivement exécuté le plan initial. Cette erreur a engendré une obligation fiscale beaucoup plus importante que prévu.

[52] Fairmont a eu vent de l'erreur à la suite d'une vérification effectuée par l'Agence du revenu du Canada. Elle a demandé à la Cour supérieure de justice de l'Ontario de rectifier les résolutions du 14 septembre 2007 par lesquelles les administrateurs avaient autorisé le rachat des actions privilégiées. Le juge Newbould a accordé la rectification de ces résolutions au motif que Fairmont n'avait jamais eu l'intention de racheter les actions privilégiées et avait toujours eu l'intention de dénouer la structure de prêts réciproques sans incidences fiscales.

[53] The Ontario Court of Appeal unanimously dismissed the appeal (Simmons, Cronk and Blair JJ.A.).

Analysis

[54] Rectification is a centuries-old equitable remedy that gave courts discretion to correct "errors in integration" if signed documents did not reflect the true intention of the parties: see John D. McCamus, *The Law of Contracts* (2nd ed. 2012), at p. 589; see also Geoff R. Hall, *Canadian Contractual Interpretation Law* (3rd ed. 2016), at pp. 188-89. Where such an error occurs, "[t]he court will therefore put the agreement right . . . to conform with the parties' true intentions" (S. M. Waddams, *The Law of Contracts* (6th ed. 2010), at p. 240).

[55] The available judicial discretion to retroactively implement the parties' true intention has been described as follows:

> The Court will not write a contract for businessmen or others but rather through the exercise of its jurisdiction to grant rectification in appropriate circumstances, it will reproduce their contract in harmony with the intention clearly manifested by them, and so defeat claims or defences which would otherwise unfairly succeed to the end that business may be fairly and ethically done . . . .

(*H. F. Clarke Ltd. v. Thermidaire Corp.*, [1973] 2 O.R. 57 (C.A.), at p. 65, per Brooke J.A., rev'd on other grounds, [1976] 1 S.C.R. 319, at pp. 323-24. See also Waddams, at pp. 240-41; G. H. L. Fridman, *The Law of Contract in Canada* (6th ed. 2011), at p. 776; McCamus, at p. 587.)

[56] While the remedy of rectification had been historically confined to cases of mutual mistake, in *Performance Industries Ltd. v. Sylvan Lake Golf & Tennis Club Ltd.*, [2002] 1 S.C.R. 678, this Court expanded its scope to include circumstances where the mistake was unilateral.

[53] La Cour d'appel de l'Ontario a rejeté l'appel à l'unanimité (les juges Simmons, Cronk et Blair).

Analyse

[54] La rectification est une réparation en equity vieille de plusieurs siècles qui confère aux tribunaux le pouvoir discrétionnaire de corriger les [TRADUCTION] « erreurs d'intégration » lorsque les documents ne reflètent pas la véritable intention des parties : voir John D. McCamus, *The Law of Contracts* (2e éd. 2012), p. 589; voir aussi Geoff R. Hall, *Canadian Contractual Interpretation Law* (3e éd. 2016), p. 188-189. En présence d'une telle erreur, [TRADUCTION] « [l]e tribunal corrige [. . .] la convention [. . .] de façon à ce qu'elle soit conforme à la véritable intention des parties » (S. M. Waddams, *The Law of Contracts* (6e éd. 2010), p. 240).

[55] Le pouvoir discrétionnaire dont dispose le tribunal de réaliser rétroactivement la véritable intention des parties a été décrit comme suit :

> [TRADUCTION] La Cour n'écrira pas un contrat pour des gens d'affaires ou autres, mais grâce à son pouvoir d'accorder une rectification lorsque les circonstances s'y prêtent, elle transposera dans leur contrat l'intention qu'ils avaient clairement exprimée et rejettera en conséquence les demandes ou moyens de défense qui pourraient être injustement accueillis en l'absence d'une rectification, afin que les affaires puissent se dérouler de façon équitable et éthique . . .

(*H. F. Clarke Ltd. c. Thermidaire Corp.*, [1973] 2 O.R. 57 (C.A.), p. 65, le juge Brooke, inf. pour d'autres motifs, [1976] 1 R.C.S. 319, p. 323-324. Voir aussi Waddams, p. 240-241; G. H. L. Fridman, *The Law of Contract in Canada* (6e éd. 2011), p. 776; McCamus, p. 587.)

[56] Bien que le recours en rectification ait depuis longtemps été limité aux cas d'erreur commune, la Cour en a étendu la portée dans *Performance Industries Ltd. c. Sylvan Lake Golf & Tennis Club Ltd.*, [2002] 1 R.C.S. 678, de façon qu'il s'applique aux cas d'erreur unilatérale.

[57] The rationale for the remedy is that no one should be allowed "to take unfair advantage of another's mistake": Lord Goff of Chieveley and Gareth Jones, *The Law of Restitution* (7th ed. 2007), at p. 299; see also Hall, at pp. 190-91. In accordance with this purpose, rectification "should not be circumscribed by anomalous or artificial rules, but should be applied where appropriate in order to give better effect to equitable doctrines": I. C. F. Spry, *The Principles of Equitable Remedies* (9th ed. 2014), at p. 632.

[58] The test for rectification requires courts to assess the true intention of the parties:

> In order for rectification to be available, it is necessary to identify a "true agreement" which precedes (and is not accurately recorded by) the written instrument. Such an agreement may itself be contained in a written instrument; but it may be oral, and need not itself have contractual force.

(*Snell's Equity* (31st ed. 2005), by John McGhee, ed., at p. 332. See also Mitchell McInnes, *The Canadian Law of Unjust Enrichment and Restitution* (2014), at p. 820; Angela Swan and Jakub Adamski, *Canadian Contract Law* (3rd ed. 2012), at pp. 772-73; Goff and Jones, at p. 295; *Hart v. Boutilier* (1916), 56 D.L.R. 20 (S.C.C.), at pp. 621-22 and 630; *Mitchell v. MacMillan* (1980), 5 Sask. R. 160 (C.A.), at para. 8; *Reed Shaw Osler Ltd. v. Wilson* (1981), 17 Alta. L.R. (2d) 81 (C.A.), at p. 89; *Bryndon Ventures Inc. v. Bragg* (1991), 82 D.L.R. (4th) 383 (B.C.C.A.), at pp. 402-3; *Dynamex Canada Inc. v. Miller* (1998), 161 Nfld. & P.E.I.R. 97 (Nfld. C.A.), at para. 23; *Wasauksing First Nation v. Wasausink Lands Inc.* (2004), 184 O.A.C. 84, at para. 77.)

[59] Nor does the parties' prior intention have to amount to a fully enforceable agreement: *Joscelyne v. Nissen*, [1970] 2 Q.B. 86 (C.A.), followed in *Peter Pan Drive-In Ltd. v. Flambro Realty Ltd.* (1978), 22 O.R. (2d) 291 (H.C.J.), aff'd (1980), 26 O.R. (2d) 746 (C.A.). As Brown J. (as he then was) explained in *Graymar Equipment (2008) Inc. v. Canada (Attorney General)* (2014), 97 Alta. L.R. (5th) 288 (Q.B.):

[57] La raison d'être du recours est que nul ne devrait pouvoir [TRADUCTION] « tirer injustement avantage de l'erreur d'autrui » : lord Goff of Chieveley et Gareth Jones, *The Law of Restitution* (7e éd. 2007), p. 299; voir aussi Hall, p. 190-191. C'est pourquoi la rectification [TRADUCTION] « devrait non pas être circonscrite par des règles incongrues ou artificielles, mais être appliquée au besoin en vue d'améliorer l'application des principes d'equity » : I. C. F. Spry, *The Principles of Equitable Remedies* (9e éd. 2014), p. 632.

[58] Le test de rectification exige des tribunaux qu'ils déterminent la véritable intention des parties :

> [TRADUCTION] Pour qu'il y ait ouverture à rectification, il est nécessaire d'établir la « véritable entente » qui précède l'écrit (et n'y est pas consignée avec exactitude). Cette entente peut elle-même être constatée par écrit, mais elle peut être verbale et n'a nullement besoin d'avoir elle-même la force d'un contrat.

(*Snell's Equity* (31e éd. 2005), par John McGhee, dir., p. 332. Voir aussi Mitchell McInnes, *The Canadian Law of Unjust Enrichment and Restitution* (2014), p. 820; Angela Swan et Jakub Adamski, *Canadian Contract Law* (3e éd. 2012), p. 772-773; Goff et Jones, p. 295; *Hart c. Boutilier* (1916), 56 D.L.R. 20 (C.S.C.), p. 621-622 et 630; *Mitchell c. MacMillan* (1980), 5 Sask. R. 160 (C.A.), par. 8; *Reed Shaw Osler Ltd. c. Wilson* (1981), 17 Alta. L.R. (2d) 81 (C.A.), p. 89; *Bryndon Ventures Inc. c. Bragg* (1991), 82 D.L.R. (4th) 383 (C.A. C.-B.), p. 402-403; *Dynamex Canada Inc. c. Miller* (1998), 161 Nfld. & P.E.I.R. 97 (C.A. T.-N.), par. 23; *Wasauksing First Nation c. Wasausink Lands Inc.* (2004), 184 O.A.C. 84, par. 77.)

[59] Il n'est pas non plus nécessaire que l'intention préalable des parties constitue une entente pleinement exécutoire : *Joscelyne c. Nissen*, [1970] 2 Q.B. 86 (C.A.), appliqué dans *Peter Pan Drive-In Ltd. c. Flambro Realty Ltd.* (1978), 22 O.R. (2d) 291 (H.C.J.), conf. par (1980), 26 O.R. (2d) 746 (C.A.). Comme l'a expliqué le juge Brown (maintenant juge de notre Cour) dans *Graymar Equipment (2008) Inc. c. Canada (Attorney General)* (2014), 97 Alta. L.R. (5th) 288 (B.R.) :

Rectification is available . . . even where the parties have not concluded an agreement, so long as there is sufficiently convincing evidence that the parties had arrived upon a common intention. [para. 36]

(See also *Snell's Equity* (33rd ed. 2015), by John McGhee, at pp. 424-25; McCamus, at p. 558; Waddams, at p. 243.)

[60] But the intention does have to be sufficiently clear and certain that courts can correct the error without resorting to speculation about what the parties had wanted to do in the first place: see *I.C.R.V. Holdings Ltd. v. Tri-Par Holdings Ltd.* (1994), 53 B.C.A.C. 72.

[61] While parties seeking rectification must provide evidence of what they actually intended, they are not required to provide "an expressed antecedent agreement in order to found a successful claim": *Peter Pan Drive-In Ltd.*, at p. 296. Courts have long recognized that "the exact form of words in which the common intention is to be expressed is immaterial" (*McLean v. McLean* (2013), 118 O.R. (3d) 216 (C.A.), at para. 46, citing *Swainland Builders Ltd. v. Freehold Properties Ltd.*, [2002] EWCA Civ 560, at para. 34 (BAILII); see also *Co-operative Insurance Society Ltd. v. Centremoor Ltd.*, [1983] 2 E.G.L.R. 52 (C.A.), at p. 54, per Dillon L.J.; *Snell's Equity* (33rd ed. 2015), at pp. 426-37). In other words, as Professor Swan explains:

. . . it is "sufficient if [the party] establishes a common continuing intention in regard to the particular provision in question". There is no need to hedge the remedy about with requirements that are no more than technical and to require precise agreement on every point in the actual agreement to prevent the court from giving relief where it is clearly justified in doing so to prevent injustice. [Footnote omitted; p. 773.]

[62] What matters instead is that the substance of the intention "can be ascertained with a reasonable level of comfort": *Performance Industries*, at para. 47. In ascertaining these intentions, courts are free to make logical inferences based on the evidence

[TRADUCTION] Il y a ouverture à rectification [. . .] même si les parties n'ont conclu aucune entente, pourvu qu'il existe une preuve suffisamment convaincante de la volonté commune des parties. [par. 36]

(Voir aussi *Snell's Equity* (33e éd. 2015), par John McGhee, p. 424-425; McCamus, p. 558; Waddams, p. 243.)

[60] Cette intention doit cependant être assez claire et certaine pour que les tribunaux puissent corriger l'erreur sans avoir à conjecturer ce que les parties voulaient faire au départ : voir *I.C.R.V. Holdings Ltd. c. Tri-Par Holdings Ltd.* (1994), 53 B.C.A.C. 72.

[61] Bien que les parties qui sollicitent la rectification doivent produire la preuve de leur véritable intention, elles ne sont pas tenues de fournir [TRADUCTION] « une entente expresse antérieure pour que leur demande soit accueillie » : *Peter Pan Drive-In Ltd.*, p. 296. Les tribunaux reconnaissent depuis longtemps que [TRADUCTION] « les termes exacts utilisés pour exprimer l'intention commune sont sans importance » (*McLean c. McLean* (2013), 118 O.R. (3d) 216 (C.A.), par. 46, citant *Swainland Builders Ltd. c. Freehold Properties Ltd.*, [2002] EWCA Civ 560, par. 34 (BAILII); voir également *Co-operative Insurance Society Ltd. c. Centremoor Ltd.*, [1983] 2 E.G.L.R. 52 (C.A.), p. 54, le lord juge Dillon; *Snell's Equity* (33e éd. 2015), p. 426-437). Autrement dit, comme l'explique la professeure Swan :

[TRADUCTION] . . . il « suffit que [la partie] établisse une intention commune constante à l'égard de la disposition précise en question ». Il n'est pas nécessaire de circonscrire la réparation par des exigences purement techniques ni d'exiger une entente précise sur chaque aspect de l'entente comme telle pour empêcher le tribunal d'accorder la réparation alors qu'il est manifestement fondé à le faire pour éviter une injustice. [Note en bas de page omise; p. 773.]

[62] En fait, ce qui importe, c'est « qu'il [soit] possible [de] dégager » la substance de l'intention « avec un degré de certitude raisonnable » : *Performance Industries*, par. 47. Pour établir cette intention, les tribunaux sont libres de tirer des conclusions logiques

before them. In *McLean*, for example, a husband and wife transferred property to their son and daughter-in-law. The wife later sought rectification of the memorandum of agreement that contained the terms of the transfer, claiming that the total purchase price was incorrect. The Ontario Court of Appeal rectified the memorandum even though it was not immediately obvious what the correct price was supposed to be. The court deduced the correct price based on "the totality of the evidence", noting that "[o]nly when the related documents are considered as a whole does the intention of the parties emerge": paras. 60 and 62. Similarly, in *Royal Bank of Canada v. El-Bris Ltd.* (2008), 92 O.R. (3d) 779 (C.A.), a business owner mistakenly signed a personal guarantee for $700,000 *and* a collateral mortgage for the same amount, when he had only intended to create one debt obligation. The Ontario Court of Appeal allowed rectification of both the guaranteed loan and the mortgage based on the true intention of the parties, even though the mechanics of the necessary corrective transactions had never been previously set out.

[63] Whether a mistake is unilateral or mutual, rectification is, ultimately, an equitable remedy that seeks to give effect to the true intention of the parties, and prevent errors from causing windfalls. The doctrine is also "based on simple notions of relief against unjust enrichment", namely, that it would be unfair to rigidly enforce an error that enriches one party at the expense of another: Waddams, at p. 240. As Professor Waddams notes, "[t]he doctrine is a far-reaching and flexible tool of justice" (p. 243). (See also McInnes, at pp. 820-21; Fridman, at pp. 782-83; *El-Bris*, at paras. 13 and 36; *McLean*, at para. 73; Patrick Hartford, "Clarifying the Doctrine of Rectification in Canada: A Comment on *Shafron v. KRG Insurance Brokers (Western) Inc.*" (2013), 54 *Can. Bus. L.J.* 87, at p. 88.)

[64] The common law principles of rectification were recently applied in *Shafron v. KRG Insurance Brokers (Western) Inc.*, [2009] 1 S.C.R. 157. *Shafron* involved an employment contract that included a

au vu de la preuve dont ils disposent. Dans *McLean*, par exemple, un mari et sa femme ont transféré leur propriété à leur fils et à leur bru. La femme a ensuite demandé la rectification du protocole d'entente qui contenait les modalités du transfert au motif que le prix d'achat total était incorrect. La Cour d'appel de l'Ontario a rectifié le protocole d'entente même si le prix qui était censé y figurer n'était pas évident à première vue. La Cour d'appel a déduit le bon prix de [TRADUCTION] « l'ensemble de la preuve » et a indiqué que « [c]e n'est que lorsque les documents connexes sont examinés dans leur ensemble que l'intention des parties se dégage » : par. 60 et 62. De même, dans l'affaire *Royal Bank of Canada c. El-Bris Ltd.* (2008), 92 O.R. (3d) 779 (C.A.), le propriétaire d'une entreprise a signé par erreur une garantie personnelle pour 700 000 $ *ainsi qu'*une hypothèque accessoire pour le même montant, alors qu'il voulait seulement créer une dette. La Cour d'appel de l'Ontario a accordé la rectification du prêt garanti et de l'hypothèque sur le fondement de la véritable intention des parties, même si les formalités des opérations correctives nécessaires n'avaient jamais été établies auparavant.

[63] Que l'erreur soit unilatérale ou commune, la rectification est, en définitive, une réparation d'equity qui vise à donner effet à la véritable intention des parties et à empêcher que des erreurs donnent lieu à des gains fortuits. La doctrine est aussi [TRADUCTION] « fondée sur de simples notions de réparation en matière d'enrichissement injustifié », à savoir qu'il serait injuste de donner effet, de façon rigide, à une erreur qui enrichit l'une des parties au détriment de l'autre : Waddams, p. 240. Comme le souligne le professeur Waddams, « [l]a doctrine est un outil de justice à la fois souple et de grande portée » (p. 243). (Voir également McInnes, p. 820-821; Fridman, p. 782-783; *El-Bris*, par. 13 et 36; *McLean*, par. 73; Patrick Hartford, « Clarifying the Doctrine of Rectification in Canada : A Comment on *Shafron v. KRG Insurance Brokers (Western) Inc.* » (2013), 54 *Rev. can. dr. comm.* 87, p. 88.)

[64] Les principes de common law en matière de rectification ont récemment été appliqués dans *Shafron c. KRG Insurance Brokers (Western) Inc.*, [2009] 1 R.C.S. 157. Cette affaire portait sur un

restrictive covenant, prohibiting Mr. Shafron from working as an insurance broker in the "Metropolitan City of Vancouver" for three years after his employment with KRG Western ended. "Metropolitan City of Vancouver" was not a legally defined term, but Mr. Shafron thought it referred to the City of Vancouver, while KRG Western thought it referred to the larger Greater Vancouver Regional District.

[65] KRG Western applied to rectify the contract by substituting "Greater Vancouver Regional District" for "Metropolitan City of Vancouver", to prevent Mr. Shafron from working as an insurance broker in the suburb of Richmond. The Court held that rectification was unavailable because KRG Western could not establish that there had been a prior agreement in which "Metropolitan City of Vancouver" was defined in sufficiently precise terms.

[66] While I acknowledge that rectification seems most often to have been granted in the context of agreed upon terms having been *transcribed* incorrectly, since unjust enrichment can also result from a mistake in *carrying out* the intention of the parties, the remedy is also available to correct errors in implementation. Courts have, as a result, granted rectification where a corporate transaction was conducted in the wrong sequence (*GT Group Telecom Inc., Re* (2004), 5 C.B.R. (5th) 230 (Ont. S.C.J.)), where an underlying calculation in a contract was incorrect (*Oriole Oil & Gas Ltd. v. American Eagle Petroleums Ltd.* (1981), 27 A.R. 411 (C.A.)), and where the requisite steps of an amalgamation were not correctly carried out (*Prospera Credit Union, Re* (2002), 32 B.L.R. (3d) 145 (B.C.S.C.)).

[67] Whether the errors are in transcription or in implementation, courts may refuse to exercise their discretion where allowing rectification would prejudice the rights of third parties (*Wise v. Axford*, [1954] O.W.N. 822 (C.A.)). But the mere existence of a third party will not bar rectification. In *Augdome Corp. v. Gray*, [1975] 2 S.C.R. 354, this Court concluded that the presence of a third party is only

contrat de travail qui comportait une clause restrictive interdisant à M. Shafron de travailler à titre de courtier d'assurance dans « l'agglomération de la ville de Vancouver » pendant les trois années suivant son départ de KRG Western. L'expression « l'agglomération de la ville de Vancouver » n'était pas définie en droit, mais M. Shafron croyait qu'elle désignait la ville de Vancouver, alors que KRG Western estimait qu'elle visait le district régional de Vancouver.

[65] KRG Western a demandé que l'on rectifie le contrat en substituant les termes « district régional de Vancouver » aux termes « l'agglomération de la ville de Vancouver », afin d'empêcher M. Shafron de travailler comme courtier d'assurance dans la banlieue de Richmond. La Cour a conclu qu'il n'y avait pas ouverture à rectification parce que KRG Western ne pouvait démontrer l'existence d'une entente préalable définissant l'expression « l'agglomération de la ville de Vancouver » en termes suffisamment précis.

[66] Je reconnais que l'on semble avoir le plus souvent accordé la rectification dans des cas où les modalités convenues avaient été mal *transcrites*, puisque l'enrichissement injustifié peut également résulter d'une erreur dans la *réalisation* de l'intention des parties, mais on peut aussi recourir à la rectification pour corriger les erreurs de mise en œuvre. Les tribunaux ont donc accordé la rectification demandée lorsqu'une transaction commerciale a été exécutée dans le mauvais ordre (*GT Group Telecom Inc., Re* (2004), 5 C.B.R. (5th) 230 (C.S.J. Ont.)), lorsqu'une erreur de calcul sous-jacente au contrat a été commise (*Oriole Oil & Gas Ltd. c. American Eagle Petroleums Ltd.* (1981), 27 A.R. 411 (C.A.)), et lorsque les étapes nécessaires d'une fusion ont été mal suivies (*Prospera Credit Union, R*e (2002), 32 B.L.R. (3d) 145 (C.S. C.-B.)).

[67] Que l'erreur réside dans la transcription ou dans la mise en œuvre, les tribunaux peuvent refuser d'exercer leur pouvoir discrétionnaire si la rectification serait préjudiciable aux droits des tiers (*Wise c. Axford*, [1954] O.W.N. 822 (C.A.)). Toutefois, la simple présence d'un tiers ne fait pas obstacle à la rectification. Dans l'arrêt *Augdome Corp. c. Gray*, [1975] 2 R.C.S. 354, la Cour a conclu que la

a bar to rectification where the third party has actually relied on the flawed agreement. This principle was subsequently explained by Gray J. in *Consortium Capital Projects Inc. v. Blind River Veneer Ltd.* (1988), 63 O.R. (2d) 761 (H.C.J.), at p. 766, aff'd (1990), 72 O.R. (2d) 703 (C.A.): ". . . the proper test is whether the third party relied on the document as executed and took action based on that document". (See also McCamus, at p. 595; Spry, at pp. 630-31; *Kolias v. Owners: Condominium Plan 309 CDC* (2008), 440 A.R. 389 (C.A.); *Carlson, Carlson and Hettrick v. Big Bud Tractor of Canada Ltd.* (1981), 7 Sask. R. 337 (C.A.), at paras. 24-26.)

[68] This is consistent with one of the underlying purposes of rectification, namely to prevent unjust enrichment: Waddams, at p. 240; *El-Bris*, at paras. 13 and 36; *McLean*, at para. 73. Just as rectification can prevent one party from enforcing an error and being unjustly enriched by the other's mistake, rectification can also prevent a third party who has not relied on the agreement from enforcing a mistake and receiving a windfall. This theory was on display in *Love v. Love*, [2013] 5 W.W.R. 662 (Sask. C.A.). The Saskatchewan Court of Appeal allowed the rectification of a life insurance contract, in which a husband had designated his wife as the beneficiary of his life insurance policy. When the couple divorced, the husband completed a new form to designate his son as the policy's beneficiary instead of his former wife. He filled the paperwork out incorrectly. After he died, the former wife and the son both attempted to claim the proceeds of the insurance policy. The court rectified the contract to reflect what it saw as the husband's true intention, namely to designate his son as the beneficiary.

[69] This brings us to the tax context.

[70] Allowing the tax authorities, a third party, to profit from legitimate tax planning errors, when its own rights have not been prejudiced in any way, amounts to unjust enrichment. Businesses and individuals are legally entitled to structure their affairs in a way that minimizes their tax burden. The General

présence d'un tiers ne fait obstacle à la rectification que si le tiers en question s'est effectivement fondé sur l'entente erronée. Le juge Gray a ultérieurement expliqué ce principe dans la décision *Consortium Capital Projects Inc. c. Blind River Veneer Ltd.* (1988), 63 O.R. (2d) 761 (H.C.J.), p. 766, conf. par (1990), 72 O.R. (2d) 703 (C.A.) : [TRADUCTION] « . . . le critère applicable est celui de savoir si le tiers s'est fondé sur le document signé et s'il a agi sur la foi de ce document ». (Voir aussi McCamus, p. 595; Spry, p. 630-631; *Kolias c. Owners : Condominium Plan 309 CDC* (2008), 440 A.R. 389 (C.A.); *Carlson, Carlson and Hettrick c. Big Bud Tractor of Canada Ltd.* (1981), 7 Sask. R. 337 (C.A.), par. 24-26.)

[68] Ce principe respecte l'un des objectifs sous-jacents de la rectification, à savoir prévenir l'enrichissement injustifié : Waddams, p. 240; *El-Bris*, par. 13 et 36; *McLean*, par. 73. La rectification peut empêcher une partie de donner effet à une erreur et de s'enrichir injustement parce que l'autre partie s'est trompée, tout comme elle peut empêcher un tiers qui ne s'est pas fié sur l'entente de donner effet à une erreur et d'en tirer profit. Cette théorie a été exposée dans l'arrêt *Love c. Love*, [2013] 5 W.W.R. 662 (C.A. Sask.). La Cour d'appel de la Saskatchewan a autorisé la rectification d'un contrat d'assurance-vie dans lequel le mari avait désigné son épouse à titre de bénéficiaire. Lorsque le couple a divorcé, le mari a rempli un nouveau formulaire afin de désigner son fils plutôt que son ex-épouse à titre de bénéficiaire. Il s'est trompé en remplissant le document. Après son décès, son ex-femme et son fils ont tous deux réclamé le produit de la police d'assurance. La cour a rectifié le contrat pour qu'il exprime ce qu'elle estimait être la véritable intention du mari, soit désigner son fils comme bénéficiaire.

[69] Passons maintenant au contexte fiscal.

[70] Permettre aux autorités fiscales, une tierce partie, de tirer profit des erreurs commises dans une planification fiscale légitime, alors qu'il n'a été nullement porté atteinte à ses droits, équivaut à un enrichissement injustifié. Les entreprises et les particuliers ont légalement le droit d'organiser

Anti-Avoidance Rule in s. 245 of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.), for example, permits transactions that are primarily designed to avoid taxes so long as they do not circumvent the *Act* in an abusive manner: *Copthorne Holdings Ltd. v. Canada*, [2011] 3 S.C.R. 721, at para. 32. There is, as a result, an inherent unfairness in enforcing errors in transcription or implementation that result in allowing the tax authorities to collect a windfall.

[71] It is true that a taxpayer should expect to be taxed based on what is actually done, not based on what could have been done (*Shell Canada Ltd. v. Canada*, [1999] 3 S.C.R. 622, at para. 45), but this principle does not deprive equity of a role where what a party or parties genuinely intended to do was transcribed *or* implemented incorrectly.

[72] On the other hand, parties should not be given *carte blanche* to exploit rectification for purposes of engaging in retroactive tax planning. Courts will not permit parties to undo decisions simply because they have come to regret them later. Allowing parties to rewrite documents and restructure their affairs based solely on a generalized and all-encompassing preference for paying lower taxes is not consistent with the equitable principles that inform rectification.

[73] As the trial judge noted in *Kanji v. Canada (Attorney General)* (2013), 114 O.R. (3d) 1 (S.C.J.), "[t]ax-driven claims for rectification must be approached with care since common sense tells us that most taxpayers would like to minimize the amount of tax they must pay to the government": para. 36. The British Columbia Court of Appeal expressed similar views in *Pallen Trust, Re* (2015), 385 D.L.R. (4th) 499, when it said:

Carrying out a fact-focussed analysis should ensure that the "social evil" of aggressive tax avoidance can, where it is just to do so, be appropriately disincentivized, and

leurs affaires de manière à réduire le plus possible leur fardeau fiscal. La règle générale anti-évitement prévue à l'art. 245 de la *Loi de l'impôt sur le revenu*, L.R.C. 1985, c. 1 (5e suppl.), par exemple, permet les opérations qui visent avant tout à éviter l'impôt, pour autant qu'elles ne contournent pas la *Loi* de manière abusive : *Copthorne Holdings Ltd. c. Canada*, [2011] 3 R.C.S. 721, par. 32. Il est donc intrinsèquement inéquitable de donner effet à une erreur de transcription ou de mise en œuvre qui permettrait aux autorités fiscales de réaliser un gain fortuit.

[71] Certes, le contribuable doit s'attendre à être imposé en fonction de ce qu'il a fait, et non de ce qu'il aurait pu faire (*Shell Canada Ltée c. Canada*, [1999] 3 R.C.S. 622, par. 45), mais ce principe n'empêche pas l'equity de jouer un rôle lorsque la véritable intention d'une ou des parties a été mal transcrite *ou* réalisée.

[72] Par contre, les parties ne devraient pas pouvoir recourir sans restriction à la rectification pour procéder à une planification fiscale rétroactive. Les tribunaux ne permettront pas aux parties de revenir sur leurs décisions simplement parce qu'elles les regrettent après coup. Le fait de permettre aux parties de réécrire des documents et de réorganiser leurs affaires simplement parce qu'elles préfèrent généralement et globalement payer moins d'impôt n'est pas compatible avec les principes d'equity qui régissent la rectification.

[73] Comme l'a signalé le juge de première instance dans la décision *Kanji c. Canada (Attorney General)* (2013), 114 O.R. (3d) 1 (C.S.J.), [TRADUCTION] « [i]l faut aborder avec prudence les demandes de rectification fondées sur des raisons fiscales, car le bon sens nous indique que la plupart des contribuables aimeraient réduire le plus possible l'impôt à payer au gouvernement » : par 36. La Cour d'appel de la Colombie-Britannique a exprimé des opinions semblables dans *Pallen Trust, Re* (2015), 385 D.L.R. (4th) 499 :

[TRADUCTION] Une analyse axée sur les faits devrait permettre d'enrayer le « fléau social » qu'est l'évitement fiscal agressif, lorsqu'il est juste de le faire, tout en ne

on the other hand that where the taxpayer's conduct has been reasonable . . . he or she is not unfairly penalized . . . . [para. 53]

[74] How then should rectification be seen in the tax context? In my view, the two most helpful common law cases on rectification in the tax context were decided by the Ontario Court of Appeal. In *771225 Ontario Inc. v. Bramco Holdings Co.* (1995), 21 O.R. (3d) 739 (C.A.), a purchaser utilized a company she owned to buy property, intending to minimize her personal income tax. She erroneously thought that her company was an Ontario company and assumed that she would pay the residential land transfer tax rate of 2 percent. The company, it turned out, was subject to the higher rate of 20 percent. This mistake resulted in a liability of $1.7 million instead of $84,745. The court denied rectification on the grounds that this was an "attemp[t] to rewrite history in order to obtain more favourable tax treatment" (p. 742). The purchaser intended the transaction to minimize her income tax — which it did — and was simply caught off-guard by land transfer tax consequences.

[75] A different result occurred in *Canada (Attorney General) v. Juliar* (2000), 50 O.R. (3d) 728 (C.A.). Two couples co-owned a company through which they operated a convenience store chain. They decided to split the business into two separate corporations so that each couple could operate independently. They mistakenly believed, based on an erroneous assumption by their tax advisor, that this would not trigger any immediate income taxes. When it did, they applied for rectification. Austin J.A. granted the remedy, stating:

. . . the true agreement between the parties here was the acquisition of the half interest in the . . . tobacco business . . . in a manner that would not attract immediate liability for income tax.

pénalisant pas injustement le contribuable dont le comportement est raisonnable . . . [par. 53]

[74] Comment alors la rectification devrait-elle être vue dans le domaine fiscal? À mon avis, les deux affaires de common law les plus instructives en la matière ont été tranchées par la Cour d'appel de l'Ontario. Dans *771225 Ontario Inc. c. Bramco Holdings Co.* (1995), 21 O.R. (3d) 739 (C.A.), une femme avait acquis un bien immeuble en se servant d'une société dont elle était propriétaire, car elle voulait réduire le plus possible son impôt sur le revenu. Croyant à tort qu'il s'agissait d'une société ontarienne, elle a présumé qu'elle paierait le taux d'imposition de 2 pour 100 applicable aux cessions de biens-fonds affectés à l'habitation. Il s'est avéré que la société était assujettie à un taux de 20 pour 100. Cette erreur s'est traduite par une dette de 1,7 million de dollars plutôt que de 84 745 dollars. La cour a refusé la rectification au motif qu'il s'agissait d'une [TRADUCTION] « tentative de réécrire l'histoire afin d'obtenir un traitement fiscal plus favorable » (p. 742). L'acheteuse voulait que cette opération génère le moins d'impôt possible sur son revenu — ce qui s'est produit — et a simplement été prise de court par les droits de cession immobilière qui en ont résulté.

[75] La Cour d'appel est parvenue à un résultat différent dans l'arrêt *Canada (Attorney General) c. Juliar* (2000), 50 O.R. (3d) 728. Deux couples exploitaient une chaîne de dépanneurs par l'entremise d'une société dont ils étaient copropriétaires. Ils ont décidé de séparer l'entreprise entre deux sociétés distinctes de sorte que chaque couple puisse agir de façon indépendante. Ils ont cru à tort, sur le fondement d'une prémisse erronée de leur conseiller fiscal, que l'opération ne générerait sur-le-champ aucun impôt sur le revenu. Constatant qu'elle en générait un, ils ont présenté une demande de rectification. Le juge Austin a accueilli la demande, affirmant ce qui suit :

[TRADUCTION] . . . la véritable entente intervenue entre les parties en l'espèce portait sur l'acquisition de la moitié de la participation dans [. . .] l'entreprise de tabac [. . .] d'une manière qui ne génère immédiatement aucun impôt sur le revenu.

. . .

. . . The plain and obvious fact . . . is that the proposed division had to be carried out on a no immediate tax basis or not at all. [paras. 25 and 27]

[76] The Court of Appeal distinguished this case from *Bramco* on the grounds that the couples' intention to avoid income tax was a primary and continuing objective of the transaction, whereas in *Bramco* the concern over the land transfer tax arose only after the transaction had been completed.

[77] I am aware that this distinction has attracted some negative commentary: Lionel Smith, "Can I Change My Mind? Undoing Trustee Decisions" (2008), 27 *E.T.P.J.* 284, at pp. 289-90; Swan and Adamski, at pp. 768-69. But in my view, the Court of Appeal's decision to allow rectification in *Juliar* can easily be explained by — and flows seamlessly from — the factual findings of the Application Judge in that case. In particular, the decision to grant rectification resulted from the factual finding that the Juliars had a continuing, ascertainable intention to pursue the transaction on a tax-free basis or not at all. Seen in this way, *Juliar* did not relax the standards for rectification in the tax context. Rather, it represents a straightforward application of the test for rectification: see Joel Nitikman, "Many Questions (and a Few Possible Answers) About the Application of Rectification in Tax Law" (2005), 53 *Can. Tax J.* 941, at p. 963.

[78] Nor do I accept the floodgates concern that courts will be unable to distinguish between legitimate mistakes and attempts at retroactive tax planning. Those courts which have applied *Juliar* appear to have very comfortably recognized the distinction. Sometimes rectification was granted (see *McPeake v. Canada (Attorney General)*, [2012] 4 C.T.C. 203 (B.C.S.C.), at paras. 21-22 and 46; *Slate Management Corp. v. Canada (Attorney General)*, 2016 ONSC 4216, at paras. 10 and 16 (CanLII); *Fraser Valley Refrigeration, Re*, [2009] 6 C.T.C. 73 (B.C.S.C.), at paras. 22-24 and 48, aff'd (2009), 280 B.C.A.C. 317). But at other times, it was denied

. . .

. . . De toute évidence [. . .] le partage proposé devait être réalisé sans conséquence fiscale immédiate, ou ne pas être réalisé du tout. [par. 25 et 27]

[76] La Cour d'appel a établi une distinction entre cette affaire et *Bramco*, expliquant que, dans le premier cas, l'intention des couples d'échapper à l'impôt sur le revenu était l'objectif premier et continu de l'opération, alors que dans l'affaire *Bramco*, la question des droits de cession immobilière ne s'est posée qu'une fois l'opération menée à terme.

[77] Je sais que cette distinction a suscité quelques commentaires négatifs : Lionel Smith, « Can I Change My Mind? Undoing Trustee Decisions » (2008), 27 *E.T.P.J.* 284, p. 289-290; Swan et Adamski, p. 768-769. J'estime toutefois que la décision de la Cour d'appel d'autoriser la rectification dans *Juliar* s'explique facilement par les conclusions de fait du juge saisi de la demande et découle naturellement de ces conclusions. En particulier, la décision d'accorder la rectification repose sur la conclusion de fait que les Juliar avaient l'intention constante et déterminable de réaliser l'opération sans incidences fiscales, ou de ne pas la réaliser du tout. Vu sous cet angle, l'arrêt *Juliar* n'a pas assoupli les normes d'application de la rectification dans le domaine fiscal. Il s'agit plutôt d'un cas d'application pure et simple du test de rectification : voir Joel Nitikman, « Many Questions (and a Few Possible Answers) About the Application of Rectification in Tax Law » (2005), 53 *Rev. fisc. can.* 941, p. 963.

[78] Je ne crois pas non plus que les tribunaux seront submergés par les demandes et incapables de faire la distinction entre les erreurs légitimes et les tentatives de planification fiscale rétroactive. Les tribunaux qui ont appliqué l'arrêt *Juliar* semblent avoir reconnu fort aisément cette distinction. La rectification a parfois été accordée (voir *McPeake c. Canada (Attorney General)*, [2012] 4 C.T.C. 203 (C.S. C.-B.), par. 21-22 et 46; *Slate Management Corp. c. Canada (Attorney General)*, 2016 ONSC 4216, par. 10 et 16 (CanLII); *Fraser Valley Refrigeration, Re*, [2009] 6 C.T.C. 73 (C.S. C.-B.), par. 22-24 et 48, conf. par (2009), 280 B.C.A.C. 317). Mais elle a été

because, while the parties had a general desire to minimize their tax burden, they could not prove that the tax objective was an intended and fundamental aspect of the transaction: *Birch Hill Equity Partners Management Inc. v. Rogers Communications Inc.* (2015), 128 O.R. (3d) 1 (S.C.J.), at paras. 32 and 40-41; *Binder v. Saffron Rouge Inc.* (2008), 89 O.R. (3d) 54 (S.C.J.), at paras. 16-18 and 22-25; *Re: Aboriginal Diamonds Group*, 2007 NWTSC 37, at paras. 38-43 (CanLII); *Zhang v. Canada (Attorney General)*, 2015 DTC 5084 (B.C.S.C.), at paras. 21 and 34; *Husky Oil Operations Ltd. v. Saskatchewan (Minister of Finance)* (2014), 443 Sask. R. 172 (Q.B.), at paras. 417 and 424-25; *JAFT Corp. v. Jones* (2014), 304 Man. R. (2d) 86 (Q.B.), at paras. 31, 39 and 43-44, aff'd (2015), 323 Man. R. (2d) 57 (C.A.); *Capstone Power Corp. v. 1177719 Alberta Ltd.*, 2016 BCSC 1274, at paras. 27-54 (CanLII); *Kanji*, at paras. 22 and 33.

[79] This brings us to this Court's most recent, and in my view most pertinent, discussion of rectification in the tax context in the companion appeals of *AES* and *Riopel*: *Quebec (Agence du revenu) v. Services Environnementaux AES inc.*, [2013] 3 S.C.R. 838. Although LeBel J. expressly declined to comment on *Juliar* because he was applying the *Civil Code of Québec*, he took an approach to the rectification of tax planning errors consistent with *Juliar*.

[80] In *AES*, the company underwent a reorganization which involved transferring 25 percent of its shares to a subsidiary. It intended that this transaction be tax-neutral, but AES's advisors made an error when calculating the value of the shares, resulting in a large, unintended, and entirely avoidable tax liability. Similarly, in the companion appeal of *Riopel*, a couple attempted to amalgamate two companies. To minimize taxes, they structured the amalgamation in a particular sequence of transactions that involved selling shares, and issuing new shares and promissory notes. The couple's tax advisors erroneously enacted the sequence out of order, resulting in a significant tax liability. LeBel J. explained that under the *Code*, if the true intention is

refusée dans d'autres cas lorsque les parties, qui souhaitaient de façon générale réduire au minimum leur fardeau fiscal, n'avaient pu démontrer que l'objectif fiscal constituait un aspect délibéré et fondamental de l'opération (*Birch Hill Equity Partners Management Inc. c. Rogers Communications Inc.* (2015), 128 O.R. (3d) 1 (C.S.J.), par. 32 et 40-41; *Binder c. Saffron Rouge Inc.* (2008), 89 O.R. (3d) 54 (C.S.J.), par. 16-18 et 22-25; *Re : Aboriginal Diamonds Group*, 2007 NWTSC 37, par. 38-43 (CanLII); *Zhang c. Canada (Attorney General)*, 2015 DTC 5084 (C.S. C.-B.), par. 21 et 34; *Husky Oil Operations Ltd. c. Saskatchewan (Minister of Finance)* (2014), 443 Sask. R. 172 (B.R.), par. 417 et 424-425; *JAFT Corp. c. Jones* (2014), 304 Man. R. (2d) 86 (B.R.), par. 31, 39 et 43-44, conf. par (2015), 323 Man. R. (2d) 57 (C.A.); *Capstone Power Corp. c. 1177719 Alberta Ltd.*, 2016 BCSC 1274, par. 27-54 (CanLII); *Kanji*, par. 22 et 33).

[79] Cela nous amène à l'analyse la plus récente et, selon moi, la plus pertinente à laquelle la Cour s'est livrée sur la rectification en matière fiscale dans les pourvois connexes *AES* et *Riopel* (*Québec (Agence du revenu) c. Services Environnementaux AES inc.*, [2013] 3 R.C.S. 838). Bien que le juge LeBel ait expressément refusé de commenter l'arrêt *Juliar* parce qu'il appliquait le *Code civil du Québec*, l'approche qu'il a adoptée à l'égard de la rectification des erreurs de planification fiscale s'accorde avec cet arrêt.

[80] Dans l'affaire *AES*, la société a fait l'objet d'une restructuration dans le cadre de laquelle elle avait convenu de céder 25 pour 100 de ses actions à une filiale. Elle voulait que l'opération n'entraîne aucune incidence fiscale, mais ses conseillers ont commis une erreur en calculant la valeur des actions, de sorte qu'elle s'est retrouvée avec une obligation fiscale importante, non voulue et entièrement évitable. De même, dans l'affaire connexe *Riopel*, un couple cherchait à fusionner deux sociétés. Afin de réduire le plus possible l'impôt à payer, ils ont prévu accomplir la fusion selon un ordre donné d'opérations comprenant la vente d'actions et l'émission de nouvelles actions et de billets à ordre. Les conseillers fiscaux du couple ont procédé sans suivre l'ordre donné, ce

erroneously expressed in writing, courts will rectify the mistake as long as the intention was sufficiently precise:

> . . . the dispute in the two appeals before us necessarily concerns the [Agence du revenu du Québec] and the [Canada Revenue Agency]. Because of their situations, it must be asked whether they can rely on acquired rights to have an erroneous writing continue to apply even though the existence of an error has been established and it has been shown that the documents filed with the tax authorities are inconsistent with the parties' true intention.
>
> . . .
>
> . . . For now, therefore, what must be determined is the true nature of the operations transacted in *AES* and *Riopel*. . . . This Court must decide whether the parties' juridical acts, which led to the notices of assessment, are consistent with their true common intention and whether the tax authorities are entitled to have an erroneous declaration of intention continue to apply. [paras 44-46]

[81] Rectification was granted in both *AES* and *Riopel* based on these principles. As LeBel J. explained, "the agreements between the parties in both appeals were validly formed in that . . . they provided for obligations whose objects were sufficiently determinable": para. 54.

[82] LeBel J. concluded that "the tax authorities do not have an acquired right to benefit from an error made by the parties to a contract after the parties have corrected the error by mutual consent": *AES*, at para. 52. In other words, the tax authorities were not entitled to get a windfall from the errors. But he also warned that these principles do not allow parties to engage in retroactive tax planning:

> Taxpayers should not view this recognition of the primacy of the parties' internal will — or common intention — as an invitation to engage in bold tax planning on the assumption that it will always be possible for them to redo their contracts retroactively should that planning fail. [para. 54]

qui a entraîné une obligation fiscale importante. Le juge LeBel a expliqué que, selon le *Code*, lorsque la véritable intention est mal exprimée par écrit, les tribunaux corrigeront l'erreur pour autant que l'intention soit suffisamment précise :

> . . . le débat en cours dans les deux appels que nous examinons concerne nécessairement l'[Agence du revenu du Québec] et l'[Agence du revenu du Canada]. En raison de leur position, il faut se demander si elles peuvent invoquer des droits acquis au maintien d'un écrit erroné, même si l'existence d'une erreur est établie et s'il est démontré que les documents transmis au fisc ne correspondent pas à la volonté réelle des parties.
>
> . . .
>
> . . . Il faut donc pour l'instant déterminer la nature réelle des opérations effectuées dans les affaires *AES* et *Riopel*. [. . .] Notre Cour doit décider si les actes juridiques accomplis par les parties et qui sont à l'origine des avis de cotisation correspondent à l'intention réelle commune des parties et si le fisc a droit au maintien d'une déclaration de volonté erronée. [par. 44-46]

[81] Partant de ces principes, la Cour a accordé la rectification tant dans *AES* que dans *Riopel.* Comme l'a expliqué le juge LeBel, « dans les deux appels, les ententes entre les parties s'étaient valablement formées, puisqu'elles prévoyaient des obligations aux objets suffisamment déterminables » (par. 54).

[82] Le juge LeBel a conclu que « le fisc ne possède pas de droit acquis au bénéfice d'une erreur que les parties à un contrat auraient commise, puis corrigée de consentement mutuel » (*AES*, par. 52). En d'autres termes, le fisc ne pouvait tirer un gain fortuit des erreurs. Or, il a également souligné que ces principes n'autorisent pas les parties à se lancer dans une planification fiscale rétroactive :

> En effet, les contribuables ne devraient pas interpréter cette reconnaissance de la primauté de la volonté interne — ou intention commune — des parties comme une invitation à se lancer dans des planifications fiscales audacieuses, en se disant qu'il leur sera toujours possible de refaire leurs contrats rétroactivement en cas d'échec de ces planifications. [par. 54]

[83] The requirements for rectification in the tax context articulated in *AES* are, in my respectful view, functionally equivalent to the test under the common law. Civil law and common law rectification in the tax context are clearly based on analogous principles, namely, that the true intention of the parties has primacy over errors in the transcription or implementation of that agreement, subject to a need for precision and the rights of third parties who detrimentally rely on the agreement.

[84] That means that there is no principled basis in either the common or civil law for a stricter standard in the tax context simply because it is the government which is positioned to benefit from a mistake. The tax department is not entitled to play "Gotcha" any more than any other third party who did not rely to its detriment on the mistake.

[85] Notably, both *AES* and *Riopel* involved errors of implementation: the error in *AES* was a faulty calculation and the error in *Riopel* was that a complex transaction was conducted in the wrong sequence. The application of rectification in these circumstances clearly confirms that rectification is *not* confined only to correcting terms that were omitted, accidentally added, or articulated incorrectly in a written document, but is no less available when the parties' true intention is erroneously implemented.

[86] In the case before us, as the Application Judge noted, this was not a situation where Fairmont merely misapprehended the consequences of unwinding the reciprocal loan structure with a share redemption. Newbould J. made explicit findings of fact that Fairmont had a continuing intention *never* to unwind the reciprocal loan structure by redeeming the preferred shares, because doing so would trigger taxable exchange gains or losses. The parties, he concluded, were aware that unwinding the reciprocal loan structure with a share redemption would trigger a substantial tax liability, and expressly agreed in emails and in-person discussions that "no redemption of the preferred shares should occur at any time". They agreed to decide at a later date what

[83] Les conditions de rectification en matière fiscale qui sont énoncées dans *AES* sont, à mon humble avis, fonctionnellement équivalentes au critère de la common law. La rectification en droit civil et celle en common law dans le domaine fiscal sont manifestement fondées sur des principes analogues, à savoir que la véritable intention des parties l'emporte sur les erreurs de transcription ou de mise en œuvre de l'entente en question, sous réserve des précisions nécessaires et des droits des tiers qui se fondent à leur détriment sur l'entente.

[84] Ainsi, aucune raison de principe ne permet, en common law ou en droit civil, d'imposer une norme plus stricte dans le domaine fiscal du simple fait que c'est le gouvernement qui pourrait bénéficier d'une erreur. Le fisc ne peut pas plus jouer à « *Gotcha* » que n'importe quel autre tiers qui ne s'est pas fondé à son détriment sur l'erreur.

[85] Signalons que les affaires *AES* et *Riopel* portaient toutes deux sur des erreurs de mise en œuvre : dans *AES*, l'erreur tenait à un mauvais calcul, et dans *Riopel*, à l'ordre erroné dans lequel on avait procédé à une opération complexe. L'application de la rectification dans ces circonstances confirme clairement que cette réparation *ne* permet *pas* uniquement de corriger les modalités qui ont été omises, ajoutées par inadvertance ou formulées incorrectement dans un document écrit, mais qu'elle s'applique tout autant lorsque la véritable intention des parties a été mal réalisée.

[86] Dans l'affaire qui nous occupe, comme l'a souligné le juge saisi de la demande, Fairmont ne s'est pas simplement méprise sur les conséquences qu'occasionnerait le dénouement de la structure de prêts réciproques au moyen d'un rachat d'actions. Le juge Newbould a expressément tiré la conclusion de fait que Fairmont avait toujours eu l'intention de ne *jamais* dénouer cette structure en rachetant les actions privilégiées, parce que cela entraînerait des gains ou des pertes sur change imposables. Les parties, a-t-il conclu, savaient qu'en dénouant la structure de prêts réciproques par un rachat d'actions, elles se retrouveraient avec une importante obligation fiscale, et elles avaient expressément convenu, par des échanges de courriels et en personne,

the exact mechanics of unwinding the reciprocal loan structure in a tax-neutral way would be.

[87] Relying on this evidence, Newbould J. concluded that

> there was a continuing intention on the part of Fairmont from the time of the 2002 loan arrangements with Legacy that the loan arrangements would be carried out with a view to being tax and accounting neutral *and a continuing intention from the time of the 2006 transaction in which control of Fairmont passed to the purchaser of its shares that the preference shares of [Fairmont's subsidiaries] would not be redeemed in light of the modified plan that was carried out at that time*.
>
> I also think a fair conclusion from the evidence . . . that when the 2006 transaction was undertaken, Fairmont had an intent that at some point in the future they would have to deal with the unhedged position of [Fairmont's subsidiaries] in a way that would be tax and accounting neutral although they had no specific plan as to how they would do that. [Emphasis added.]

((2014), 123 O.R. (3d) 241, at paras. 32-33)

[88] Newbould J. was accordingly satisfied that Fairmont had an unwavering intention to unwind the reciprocal loan structure in a way that ensured that any foreign exchange gains and losses would be offset against each other:

> In this case, the intention of Fairmont from 2002 was to carry out the reciprocal loan arrangements with Legacy on a tax and accounting neutral basis so that any foreign exchange gain would be offset by a corresponding foreign exchange loss. When control of Fairmont changed in 2006, that intention did not change and when the loan unwind occurred in 2007, that intention did not change. . . .
>
> I do not see this as a case in which tax planning has been done on a retroactive basis after a [Canada Revenue Agency] audit. The purpose of the 2007 unwind of the loans was not to redeem the preference shares of [Fairmont's subsidiaries], but to unwind the loans on a

[TRADUCTION] « [qu']aucun rachat des actions privilégiées ne devait avoir lieu à quelque moment que ce soit ». Elles avaient convenu de décider plus tard des mécanismes précis par lesquels elles dénoueraient la structure de prêts réciproques sans incidences fiscales.

[87] S'appuyant sur ces éléments de preuve, le juge Newbould a conclu :

> [TRADUCTION] . . . à la présence d'une intention constante, de la part de Fairmont, dès la conclusion des contrats de prêts avec Legacy en 2002, que l'exécution de ces contrats n'ait aucune incidence fiscale ou comptable, *ainsi qu'à une intention constante, à compter de l'opération par laquelle le contrôle de Fairmont est passé à l'acquéreur de ses actions, en 2006, que les actions privilégiées [des filiales de Fairmont] ne seraient pas rachetées eu égard au plan modifié qui était alors en voie de réalisation.*
>
> En toute équité, je crois pouvoir aussi conclure de la preuve [. . .] qu'en 2006, au moment de procéder à l'opération, Fairmont entendait régler ultérieurement le problème de la position non couverte de [ses filiales] sans incidences fiscales ou comptables, tout en n'ayant aucune idée précise de la façon dont elle s'y prendrait. [Italiques ajoutés.]

((2014), 123 O.R. (3d) 241, par. 32-33)

[88] Le juge Newbould était donc convaincu que Fairmont avait fait preuve d'une intention inébranlable de dénouer la structure de prêts réciproques de façon à ce qu'il y ait compensation entre les gains et les pertes sur change :

> [TRADUCTION] En l'espèce, l'intention de Fairmont était, depuis 2002, d'exécuter les contrats de prêts réciproques conclus avec Legacy sans incidences fiscales ou comptables, de sorte que tous les gains sur change soient compensés par les pertes sur change correspondantes. Lorsque le contrôle de Fairmont a changé de mains, en 2006, cette intention est restée la même, et lorsque le dénouement des prêts a été réalisé, en 2007, cette intention est restée la même. . .
>
> Je ne considère pas que nous sommes en présence d'une affaire où l'on se serait livré rétroactivement à une planification fiscale après une vérification de l'[Agence du revenu du Canada]. L'objet du dénouement des prêts réalisé en 2007 n'était pas de racheter les actions privilégiées

tax-free basis. The redemption of the preference shares was mistakenly chosen as the means to do so. [paras. 42-43]

[89] This means that Fairmont was not attempting to change its original intention because of unanticipated tax consequences. It *had* anticipated the tax consequences of unwinding the reciprocal loan structure with a preferred share redemption, and it rejected this course of action.

[90] Fairmont was found by Newbould J. to have always had a clear, continuing intention to unwind the reciprocal loan structure on a tax-neutral basis and never to redeem the preferred shares. But, by mistake, the preferred share redemption terms were included in the directors' resolutions. This is exactly the kind of mistake rectification exists to remedy. Once Newbould J. was satisfied of the true intention of the parties, he was entitled to give effect to it by allowing the replacement loan arrangement terms to be inserted into the directors' resolutions.

[91] To require an exhaustive account of how the transaction was supposed to have proceeded would amount to imposing a uniquely high threshold for rectification in the tax context. As Newbould J. explained, denying the application to rectify the agreement in these circumstances would "give [the Canada Revenue Agency] an unintended gain because of the mistake": para. 44. There is no basis for permitting a windfall to the Canada Revenue Agency that no other third party would have been entitled to.

[92] I would dismiss the appeal with costs.

Appeal allowed with costs, ABELLA *and* CÔTÉ JJ. *dissenting.*

Solicitor for the appellant: Attorney General of Canada, Ottawa.

Solicitors for the respondents: McCarthy Tétrault, Toronto.

des [filiales de Fairmont], mais de dénouer les prêts sans incidences fiscales. C'est par erreur que l'on a choisi de le faire par le rachat des actions privilégiées. [par. 42-43]

[89] Cela signifie que Fairmont ne tentait pas de s'écarter de son intention initiale à cause de conséquences fiscales imprévues. Elle *avait* prévu les conséquences fiscales d'un dénouement de la structure de prêts réciproques par le rachat des actions privilégiées, et elle avait rejeté cette démarche.

[90] Selon le juge Newbould, Fairmont a plutôt toujours eu l'intention claire de dénouer la structure de prêts réciproques sans incidences fiscales et n'a jamais eu l'intention de racheter les actions privilégiées. Or, par erreur, les modalités de rachat des actions privilégiées ont été incluses dans les résolutions adoptées par les administrateurs. C'est exactement le genre d'erreur que la rectification vise à corriger. Une fois que le juge Newbould a été convaincu de la véritable intention des parties, il avait le droit de lui donner effet en permettant que les modalités de remplacement du contrat de prêt soient insérées dans les résolutions des administrateurs.

[91] Exiger une description détaillée de la manière dont l'opération était censée se dérouler reviendrait à imposer un seuil exceptionnellement élevé de rectification dans le domaine fiscal. Comme le juge Newbould l'a expliqué, le fait de rejeter la demande de rectification de l'entente dans les circonstances [TRADUCTION] « permettrait à [l'Agence du revenu du Canada] de tirer un gain fortuit de l'erreur » : par. 44. Il n'y a aucune raison de permettre à l'Agence du revenu du Canada de tirer un gain fortuit auquel aucun autre tiers n'aurait eu droit.

[92] Je rejetterais le pourvoi avec dépens.

Pourvoi accueilli avec dépens, les juges ABELLA *et* CÔTÉ *sont dissidentes.*

Procureur de l'appelant : Procureur général du Canada, Ottawa.

Procureurs des intimées : McCarthy Tétrault, Toronto.

Tab 5

CITATION: Danier Leather Inc. (Re), 2016 ONSC 1044
COURT FILE NO.: 31-CL-2084381
DATE: 20160210

SUPERIOR COURT OF JUSTICE - ONTARIO

IN THE MATTER OF INTENTION TO MAKE A PROPOSAL OF DANIER LEATHER INC.

BEFORE: Penny J.

COUNSEL: *Jay Swartz* and *Natalie Renner* for Danier

Sean Zweig for the Proposal Trustee

Harvey Chaiton for the Directors and Officers

Jeffrey Levine for GA Retail Canada

David Bish for Cadillac Fairview

Linda Galessiere for Morguard Investment, 20 ULC Management, SmartReit and Ivanhoe Cambridge

Clifton Prophet for CIBC

HEARD: February 8, 2016

ENDORSEMENT

The Motion

[1] On February 8, 2016 I granted an order approving a SISP in respect of Danier Leather Inc., with reasons to follow. These are those reasons.

[2] Danier filed a Notice of Intention to make a proposal under the BIA on February 4, 2016. This is a motion to :

(a) approve a stalking horse agreement and SISP;

(b) approve the payment of a break fee, expense reimbursement and signage costs obligations in connection with the stalking horse agreement;

(c) authorize Danier to perform its obligations under engagement letters with its financial advisors and a charge to secure success fees;

(d) approve an Administration Charge;

(e) approve a D&O Charge;

(f) approve a KERP and KERP Charge; and

(g) grant a sealing order in respect of the KERP and a stalking horse offer summary.

Background

[3] Danier is an integrated designer, manufacturer and retailer of leather and suede apparel and accessories. Danier primarily operates its retail business from 84 stores located throughout Canada. It does not own any real property. Danier employs approximately 1,293 employees. There is no union or pension plan.

[4] Danier has suffered declining revenues and profitability over the last two years resulting primarily from problems implementing its strategic plan. The accelerated pace of change in both personnel and systems resulting from the strategic plan contributed to fashion and inventory miscues which have been further exacerbated by unusual extremes in the weather and increased competition from U.S. and international retailers in the Canadian retail space and the depreciation of the Canadian dollar relative to the American dollar.

[5] In late 2014, Danier implemented a series of operational and cost reduction initiatives in an attempt to return Danier to profitability. These initiatives included reductions to headcount, marketing costs, procurement costs and capital expenditures, renegotiating supply terms, rationalizing Danier's operations, improving branding, growing online sales and improving price management and inventory mark downs. In addition, Danier engaged a financial advisor and formed a special committee comprised of independent members of its board of directors to explore strategic alternatives to improve Danier's financial circumstances, including soliciting an acquisition transaction for Danier.

[6] As part of its mandate, the financial advisor conducted a seven month marketing process to solicit offers from interested parties to acquire Danier. The financial advisor contacted approximately 189 parties and provided 33 parties with a confidential information memorandum describing Danier and its business. Over the course of this process, the financial advisor had meaningful conversations with several interested parties but did not receive any formal offers to provide capital and/or to acquire the shares of Danier. One of the principal reasons that this process was unsuccessful is that it focused on soliciting an acquisition transaction, which ultimately proved unappealing to interested parties as Danier's risk profile was too great. An acquisition transaction did not afford prospective purchasers the ability to restructure Danier's affairs without incurring significant costs.

[7] Despite Danier's efforts to restructure its financial affairs and turn around its operations, Danier has experienced significant net losses in each of its most recently completed fiscal years and in each of the two most recently completed fiscal quarters in the 2016 fiscal year. Danier currently has approximately $9.6 million in cash on hand but is projected to be cash flow

negative every month until at least September 2016. Danier anticipated that it would need to borrow under its loan facility with CIBC by July 2016. CIBC has served a notice of default and indicate no funds will be advanced under its loan facility. In addition, for the 12 months ending December 31, 2015, 30 of Danier's 84 store locations were unprofitable. If Danier elects to close those store locations, it will be required to terminate the corresponding leases and will face substantial landlord claims which it will not be able to satisfy in the normal course.

[8] Danier would not have had the financial resources to implement a restructuring of its affairs if it had delayed a filing under the BIA until it had entirely used up its cash resources. Accordingly, on February 4, 2016, Danier commenced these proceedings for the purpose of entering into a stalking horse agreement and implementing the second phase of the SISP.

The Stalking Horse Agreement

[9] The SISP is comprised of two phases. In the first phase, Danier engaged the services of its financial advisor to find a stalking horse bidder. The financial advisor corresponded with 22 parties, 19 of whom had participated in the 2015 solicitation process and were therefore familiar with Danier. In response, Danier received three offers and, with the assistance of the financial advisor and the Proposal Trustee, selected GA Retail Canada or an affiliate (the "Agent") as the successful bid. The Agent is an affiliate of Great American Group, which has extensive experience in conducting retail store liquidations.

[10] On February 4, 2016, Danier and the Agent entered into the stalking horse agreement, subject to Court approval. Pursuant to the stalking horse agreement, the Agent will serve as the stalking horse bid in the SISP and the exclusive liquidator for the purpose of disposing of Danier's inventory. The Agent will dispose of the merchandise by conducting a "store closing" or similar sale at the stores.

[11] The stalking horse agreement provides that Danier will receive a net minimum amount equal to 94.6% of the aggregate value of the merchandise, provided that the value of the merchandise is no less than $22 million and no more than $25 million. After payment of this amount and the expenses of the sale, the Agent is entitled to retain a 5% commission. Any additional proceeds of the sale after payment of the commission are divided equally between the Agent and Danier.

[12] The stalking horse agreement also provides that the Agent is entitled to (a) a break fee in the amount of $250,000; (b) an expense reimbursement for its reasonable and documented out-of-pocket expenses in an amount not to exceed $100,000; and (c) the reasonable costs, fees and expenses actually incurred and paid by the Agent in acquiring signage or other advertising and promotional material in connection with the sale in an amount not to exceed $175,000, each payable if another bid is selected and the transaction contemplated by the other bid is completed. Collectively, the break fee, the maximum amount payable under the expense reimbursement and the signage costs obligations represent approximately 2.5% of the minimum consideration payable under the stalking horse agreement. Another liquidator submitting a successful bid in the course of the SISP will be required to purchaser the signage from the Agent at its cost.

[13] The stalking horse agreement is structured to allow Danier to proceed with the second phase of the SISP and that process is designed to test the market to ascertain whether a higher or better offer can be obtained from other parties. While the stalking horse agreement contemplates liquidating Danier's inventory, it also establishes a floor price that is intended to encourage bidders to participate in the SISP who may be interested in going concern acquisitions as well.

The SISP

[14] Danier, in consultation with the Proposal Trustee and financial advisor, have established the procedures which are to be followed in conducting the second phase of the SISP.

[15] Under the SISP, interested parties may make a binding proposal to acquire the business or all or any part of Danier's assets, to make an investment in Danier or to liquidate Danier's inventory and furniture, fixtures and equipment.

[16] Danier, in consultation with the Proposal Trustee and its financial advisors, will evaluate the bids and may (a) accept, subject to Court approval, one or more bids, (b) conditionally accept, subject to Court approval, one or more backup bids (conditional upon the failure of the transactions contemplated by the successful bid to close, or (c) pursue an auction in accordance with the procedures set out in the SISP.

[17] The key dates of the second phase of the SISP are as follows:

(1) The second phase of the SISP will commence upon approval by the Court

(2) Bid deadline: February 22, 2016

(3) Advising interested parties whether bids constitute "qualified bids": No later than two business days after bid deadline

(4) Determining successful bid and back-up bid (if there is no auction): No later than five business days after bid deadline

(5) Advising qualified bidders of auction date and location (if applicable): No later than five business days after bid deadline

(6) Auction (if applicable): No later than seven business days after bid deadline

(7) Bringing motion for approval: Within five business days following determination by Danier of the successful bid (at auction or otherwise)

(8) Back-Up bid expiration date: No later than 15 business days after the bid deadline, unless otherwise agreed

(9) Outside date: No later than 15 business days after the bid deadline

[18] The timelines in the SISP have been designed with regard to the seasonal nature of the business and the fact that inventory values will depreciate significantly as the spring season approaches. The timelines also ensure that any purchaser of the business as a going concern has the opportunity to make business decisions well in advance of Danier's busiest season, being fall/winter. These timelines are necessary to generate maximum value for Danier's stakeholders and are sufficient to permit prospective bidders to conduct their due diligence, particularly in light of the fact that is expected that many of the parties who will participate in the SISP also participated in the 2015 solicitation process and were given access to a data room containing non-public information about Danier at that time.

[19] Danier does not believe that there is a better viable alternative to the proposed SISP and stalking horse agreement.

[20] The use of a sale process that includes a stalking horse agreement maximizes value of a business for the benefit of its stakeholders and enhances the fairness of the sale process. Stalking horse agreements are commonly used in insolvency proceedings to facilitate sales of businesses and assets and are intended to establish a baseline price and transactional structure for any superior bids from interested parties, *CCM Master Qualified Fund Ltd.* v. *blutip Power Technologies*, 2012 ONSC 1750 at para. 7 [Commercial List].

[21] The Court's power to approve a sale of assets in a proposal proceeding is codified in section 65.13 of the BIA, which sets out a list of non-exhaustive factors for the Court to consider in determining whether to approve a sale of the debtor's assets outside the ordinary course of business. This Court has considered section 65.13 of the BIA when approving a stalking horse sale process under the BIA, *Re Colossus Minerals Inc.*, 2014 CarswellOnt 1517 at paras. 22-26 (S.C.J.).

[22] A distinction has been drawn, however, between the approval of a sale process and the approval of an actual sale. Section 65.13 is engaged when the Court determines whether to approve a sale transaction arising as a result of a sale process, it does not necessarily address the factors a court should consider when deciding whether to approve the sale process itself.

[23] In *Re Brainhunter*, the Court considered the criteria to be applied on a motion to approve a stalking horse sale process in a restructuring proceeding under the *Companies' Creditors Arrangement Act*. Citing his decision in *Nortel*, Justice Morawetz (as he then was) confirmed that the following four factors should be considered by the Court in the exercise of its discretion to determine if the proposed sale process should be approved:

(1) Is a sale transaction warranted at this time?

(2) Will the sale benefit the whole "economic community"?

(3) Do any of the debtors' creditors have a bona fide reason to object to a sale of the business?

(4) Is there a better viable alternative?

Re Brainhunter, 2009 CarswellOnt 8207 at paras. 13-17 (S.C.J. [Commercial List]); *Re Nortel Networks Corp.*, 2009 CarswellOnt 4467 at para. 49 (S.C.J. [Commercial List]).

[24] While *Brainhunter* and *Nortel* both dealt with a sale process under the CCAA, the Court has recognized that the CCAA is an analogous restructuring statute to the proposal provisions of the BIA, *Re Ted Leroy Trucking [Century Services] Ltd.*, 2010 SCC 60 at para 24; *Re Indalex Ltd.*, [2013] 1 S.C.R. 271 at paras. 50-51.

[25] Furthermore, in *Mustang*, this Court applied the *Nortel* criteria on a motion to approve a sale process backstopped by a stalking horse bid in a proposal proceeding under the BIA, *Re Mustang GP Ltd.*, 2015 CarswellOnt 16398 at paras. 37-38 (S.C.J.).

[26] These proceedings are premised on the implementation of a sale process using the stalking horse agreement as the minimum bid intended to maximize value and act as a baseline for offers received in the SISP. In the present case, Danier is seeking approval of the stalking horse agreement for purposes of conducting the SISP only.

[27] The SISP is warranted at this time for a number of reasons.

[28] First, Danier has made reasonable efforts in search of alternate financing or an acquisition transaction and has attempted to restructure its operations and financial affairs since 2014, all of which has been unsuccessful. At this juncture, Danier has exhausted all of the remedies available to it outside of a Court-supervised sale process. The SISP will result in the most viable alternative for Danier, whether it be a sale of assets or the business (through an auction or otherwise) or an investment in Danier.

[29] Second, Danier projects that it will be cash flow negative for the next six months and it is clear that Danier will be unable to borrow under the CIBC loan facility to finance its operations (CIBC gave notice of default upon Danier's filing of the NOI). If the SISP is not implemented in the immediate future, Danier's revenues will continue to decline, it will incur significant costs and the value of the business will erode, thereby decreasing recoveries for Danier's stakeholders.

[30] Third, the market for Danier's assets as a going concern will be significantly reduced if the SISP is not implemented at this time because the business is seasonal in nature. Any purchaser of the business as a going concern will need to make decisions about the raw materials it wishes to acquire and the product lines it wishes to carry by March 2016 in order to be sufficiently prepared for the fall/winter season, which has historically been Danier's busiest.

[31] Danier and the Proposal Trustee concur that the SISP and the stalking horse agreement will benefit the whole of the economic community. In particular:

(a) the stalking horse agreement will establish the floor price for Danier's inventory, thereby maximizing recoveries;

(b) the SISP will subject the assets to a public marketing process and permit higher and better offers to replace the Stalking horse agreement; and

(c) should the SISP result in a sale transaction for all or substantially all of Danier's assets, this may result in the continuation of employment, the assumption of lease and other obligations and the sale of raw materials and inventory owned by Danier.

[32] There have been no expressed creditor concerns with the SISP as such. The SISP is an open and transparent process. Absent the stalking horse agreement, the SISP could potentially result in substantially less consideration for Danier's business and/or assets.

[33] Given the indications of value obtained through the 2015 solicitation process, the stalking horse agreement represents the highest and best value to be obtained for Danier's assets at this time, subject to a higher offer being identified through the SISP.

[34] Section 65.13 of the BIA is also indirectly relevant to approval of the SISP. In deciding whether to grant authorization for a sale, the court is to consider, among other things:

(a) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;

(b) whether the trustee approved the process leading to the proposed sale or disposition;

(c) whether the trustee filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;

(d) the extent to which the creditors were consulted;

(e) the effects of the proposed sale or disposition on the creditors and other interested parties; and

(f) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

[35] In the present case, in addition to satisfying the *Nortel* criteria, the SISP will result in a transaction that is at least capable of satisfying the 65.13 criteria. I say this for the following reasons.

[36] The SISP is reasonable in the circumstances as it is designed to be flexible and allows parties to submit an offer for some or all of Danier's assets, make an investment in Danier or acquire the business as a going concern. This is all with the goal of improving upon the terms of the stalking horse agreement. The SISP also gives Danier and the Proposal Trustee the right to extend or amend the SISP to better promote a robust sale process.

[37] The Proposal Trustee and the financial advisor support the SISP and view it as reasonable and appropriate in the circumstances.

[38] The duration of the SISP is reasonable and appropriate in the circumstances having regard to Danier's financial situation, the seasonal nature of its business and the fact that many potentially interested parties are familiar with Danier and its business given their participation in the 2015 solicitation process and/or the stalking horse process.

[39] A sale process which allows Danier to be sold as a going concern would likely be more beneficial than a sale under a bankruptcy, which does not allow for the going concern option.

[40] Finally, the consideration to be received for the assets under the stalking horse agreement appears at this point, to be *prima facie* fair and reasonable and represents a fair and reasonable benchmark for all other bids in the SISP.

The Break Fee

[41] Break fees and expense and costs reimbursements in favour of a stalking horse bidder are frequently approved in insolvency proceedings. Break fees do not merely reflect the cost to the purchaser of putting together the stalking horse bid. A break fee may be the price of stability, and thus some premium over simply providing for out of pocket expenses may be expected, Daniel R. Dowdall & Jane O. Dietrich, "Do Stalking Horses Have a Place in Intra-Canadian Insolvencies", 2005 ANNREVINSOLV 1 at 4.

[42] Break fees in the range of 3% and expense reimbursements in the range of 2% have recently been approved by this Court, *Re Nortel Networks Corp.*, [2009] O.J. No. 4293 at paras. 12 and 26 (S.C.J. [Commercial List]); *Re W.C. Wood Corp. Ltd.*, [2009] O.J. No. 4808 at para. 3 (S.C.J. [Commercial List], where a 4% break fee was approved.

[43] The break fee, the expense reimbursement and the signage costs obligations in the stalking horse agreement fall within the range of reasonableness. Collectively, these charges represent approximately 2.5% of the minimum consideration payable under the stalking horse agreement. In addition, if a liquidation proposal (other than the stalking horse agreement) is the successful bid, Danier is not required to pay the signage costs obligations to the Agent. Instead, the successful bidder will be required to buy the signage and advertising material from the Agent at cost.

[44] In the exercise of its business judgment, the Board unanimously approved the break fee, the expense reimbursement and the signage costs obligations. The Proposal Trustee and the financial advisor have both reviewed the break fee, the expense reimbursement and the signage costs obligations and concluded that each is appropriate and reasonable in the circumstances. In reaching this conclusion, the Proposal Trustee noted, among other things, that:

(i) the maximum amount of the break fee, expense reimbursement and signage costs obligations represent, in the aggregate 2.5% of the imputed value of the consideration under the stalking horse agreement, which is within the normal range for transactions of this nature;

(ii) each stalking horse bidder required a break fee and expense reimbursement as part of their proposal in the stalking horse process;

(iii) without these protections, a party would have little incentive to act as the stalking horse bidder; and

(iv) the quantum of the break fee, expense reimbursement and signage costs obligations are unlikely to discourage a third party from submitting an offer in the SISP.

[45] I find the break fee to be reasonable and appropriate in the circumstances.

Financial Advisor Success Fee and Charge

[46] Danier is seeking a charge in the amount of US$500,000 to cover its principal financial advisor's (Concensus) maximum success fees payable under its engagement letter. The Consensus Charge would rank behind the existing security, *pari passu* with the Administration Charge and ahead of the D&O Charge and KERP Charge.

[47] Orders approving agreements with financial advisors have frequently been made in insolvency proceedings, including CCAA proceedings and proposal proceedings under the BIA. In determining whether to approve such agreements and the fees payable thereunder, courts have considered the following factors, among others:

(a) whether the debtor and the court officer overseeing the proceedings believe that the quantum and nature of the remuneration are fair and reasonable;

(b) whether the financial advisor has industry experience and/or familiarity with the business of the debtor; and

(c) whether the success fee is necessary to incentivize the financial advisor.

Re Sino-Forest Corp., 2012 ONSC 2063 at paras. 46-47 [Commercial List]; *Re Colossus Minerals Inc.*,*supra*.

[48] The SISP contemplates that the financial advisor will continue to be intimately involved in administering the SISP.

[49] The financial advisor has considerable experience working with distressed companies in the retail sector that are in the process of restructuring, including seeking strategic partners and/or selling their assets. In the present case, the financial advisor has assisted Danier in its restructuring efforts to date and has gained a thorough and intimate understanding of the business. The continued involvement of the financial advisor is essential to the completion of a successful transaction under the SISP and to ensuring a wide-ranging canvass of prospective bidders and investors.

[50] In light of the foregoing, Danier and the Proposal Trustee are in support of incentivizing the financial advisor to carry out the SISP and are of the view that the quantum and nature of the remuneration provided for in the financial advisor's engagement letter are reasonable in the circumstances and will incentivize the Financial advisor.

[51] Danier has also engaged OCI to help implement the SISP in certain international markets in the belief that OCI has expertise that warrants this engagement. OCI may be able to identify a purchaser or strategic investor in overseas markets which would result in a more competitive sales process. OCI will only be compensated if a transaction is originated by OCI or OCI introduces the ultimate purchaser and/or investor to Danier.

[52] Danier and the Proposal Trustee believe that the quantum and nature of the success fee payable under the OCI engagement letter is reasonable in the circumstances. Specifically, because the fees payable to OCI are dependent on the success of transaction or purchaser or investor originated by OCI, the approval of this fee is necessary to incentivize OCI.

[53] Accordingly, an order approving the financial advisor and OCI engagement letters is appropriate.

[54] A charge ensuring payment of the success fee is also appropriate in the circumstances, as noted below.

Administration Charge

[55] In order to protect the fees and expenses of each of the Proposal Trustee, its counsel, counsel to Danier, the directors of Danier and their counsel, Danier seeks a charge on its property and assets in the amount of $600,000. The Administration Charge would rank behind the existing security, *pari passu* with the Consensus Charge and ahead of the D&O Charge and KERP Charge. It is supported by the Proposal Trustee.

[56] Section 64.2 of the BIA confers on the Court the authority to grant a charge in favour of financial, legal or other professionals involved in proposal proceedings under the BIA.

[57] Administration and financial advisor charges have been previously approved in insolvency proposal proceedings, where, as in the present case, the participation of the parties whose fees are secured by the charge is necessary to ensure a successful proceeding under the BIA and for the conduct of a sale process, *Re Colossus Minerals Inc.*, 2014 CarswellOnt 1517 at paras. 11-15 (S.C.J.).

[58] This is an appropriate circumstance for the Court to grant the Administration Charge. The quantum of the proposed Administration Charge is fair and reasonable given the nature of the SISP. Each of the parties whose fees are to be secured by the Administration Charge has played (and will continue to play) a critical role in these proposal proceedings and in the SI. The Administration Charge is necessary to secure the full and complete payment of these fees. Finally, the Administration Charge will be subordinate to the existing security and does not prejudice any known secured creditor of Danier.

D&O Charge

[59] The directors and officers have been actively involved in the attempts to address Danier's financial circumstances, including through exploring strategic alternatives, implementing a turnaround plan, devising the SISP and the commencement of these proceedings. The directors and officers are not prepared to remain in office without certainty with respect to coverage for potential personal liability if they continue in their current capacities.

[60] Danier maintains directors and officers insurance with various insurers. There are exclusions in the event there is a change in risk and there is potential for there to be insufficient funds to cover the scope of obligations for which the directors and officers may be found personally liable (especially given the significant size of the Danier workforce).

[61] Danier has agreed, subject to certain exceptions, to indemnify the directors and officers to the extent that the insurance coverage is insufficient. Danier does not anticipate it will have sufficient funds to satisfy those indemnities if they were ever called upon.

[62] Danier seeks approval of a priority charge to indemnify its directors and officers for obligations and liabilities they may incur in such capacities from and after the filing of the NOI. It is proposed that the D&O Charge be in an amount not to exceed $4.9 million and rank behind the existing security, the Administration Charge and the Consensus Charge but ahead of the KERP Charge.

[63] The amount of the D&O Charge is based on payroll obligations, vacation pay obligations, employee source deduction obligations and sales tax obligations that may arise during these proposal proceedings. It is expected that all of these amounts will be paid in the normal course as Danier expects to have sufficient funds to pay these amounts. Accordingly, it is unlikely that the D&O charge will be called upon.

[64] The Court has the authority to grant a directors' and officers' charge under section 64.1 of the BIA.

[65] In *Colossus Minerals* and *Mustang, supra*, this Court approved a directors' and officers' charge in circumstances similar to the present case where there was uncertainty that the existing insurance was sufficient to cover all potential claims, the directors and officers would not continue to provide their services without the protection of the charge and the continued involvement of the directors and officers was critical to a successful sales process under the BIA.

[66] I approve the D&O Charge for the following reasons.

[67] The D&O Charge will only apply to the extent that the directors and officers do not have coverage under the existing policy or Danier is unable to satisfy its indemnity obligations.

[68] The directors and officers of Danier have indicated they will not continue their involvement with Danier without the protection of the D&O Charge yet their continued involvement is critical to the successful implementation of the SISP.

[69] The D&O Charge applies only to claims or liabilities that the directors and officers may incur after the date of the NOI and does not cover misconduct or gross negligence.

[70] The Proposal Trustee supports the D&O Charge, indicating that the D&O Charge is reasonable in the circumstances.

[71] Finally, the amount of the D&O Charge takes into account a number of statutory obligations for which directors and officers are liable if Danier fails to meet these obligations. However, it is expected that all of these amounts will be paid in the normal course. Danier expects to have sufficient funds to pay these amounts. Accordingly, it is unlikely that the D&O charge will be called upon.

Key Employee Retention Plan and Charge

[72] Danier developed a key employee retention plan (the "KERP") that applies to 11 of Danier's employees, an executive of Danier and Danier's consultant, all of whom have been determined to be critical to ensuring a successful sale or investment transaction. The KERP was reviewed and approved by the Board.

[73] Under the KERP, the key employees will be eligible to receive a retention payment if these employees remain actively employed with Danier until the earlier of the completion of the SISP, the date upon which the liquidation of Danier's inventory is complete, the date upon which Danier ceases to carry on business, or the effective date that Danier terminates the services of these employees.

[74] Danier is requesting approval of the KERP and a charge for up to $524,000 (the "KERP Charge") to secure the amounts payable thereunder. The KERP Charge will rank in priority to all claims and encumbrances other than the existing security, the Administration Charge, the Consensus Charge and the D&O Charge.

[75] Key employee retention plans are approved in insolvency proceedings where the continued employment of key employees is deemed critical to restructuring efforts, *Re Nortel Networks Corp. supra.*

[76] In *Re Grant Forest Products Inc.*, Newbould J. set out a non-exhaustive list of factors that the court should consider in determining whether to approve a key employee retention plan, including the following:

(a) whether the court appointed officer supports the retention plan;

(b) whether the key employees who are the subject of the retention plan are likely to pursue other employment opportunities absent the approval of the retention plan;

(c) whether the employees who are the subject of the retention plan are truly "key employees" whose continued employment is critical to the successful restructuring of Danier;

(d) whether the quantum of the proposed retention payments is reasonable; and

(e) the business judgment of the board of directors regarding the necessity of the retention payments.

Re Grant Forest Products Inc., [2009] O.J. No. 3344 at paras. 8-22 (S.C.J. [Commercial List]).

[77] While *Re Grant Forest Products Inc*. involved a proceeding under the CCAA, key employee retention plans have frequently been approved in proposal proceedings under the BIA, see, for example, *In the Matter of the Notice of Intention of Starfield Resources Inc.*, Court File No. CV-13-10034-00CL, Order dated March 15, 2013 at para. 10.

[78] The KERP and the KERP Charge are approved for the following reasons:

(i) the Proposal Trustee supports the granting of the KERP and the KERP Charge;

(ii) absent approval of the KERP and the KERP Charge, the key employees who are the subject of the KERP will have no incentive to remain with Danier throughout the SISP and are therefore likely to pursue other employment opportunities;

(iii) Danier has determined that the employees who are the subject of the KERP are critical to the implementation of the SISP and a completion of a successful sale or investment transaction in respect of Danier;

(iv) the Proposal Trustee is of the view that the KERP and the quantum of the proposed retention payments is reasonable and that the KERP Charge will provide security for the individuals entitled to the KERP, which will add stability to the business during these proceedings and will assist in maximizing realizations; and

(v) the KERP was reviewed and approved by the Board.

Sealing Order

[79] There are two documents which are sought to be sealed: 1) the details about the KERP; and 2) the stalking horse offer summary.

[80] Section 137(2) of the *Courts of Justice Act* provides the court with discretion to order that any document filed in a civil proceeding can be treated as confidential, sealed, and not form part of the public record.

[81] In *Sierra Club of Canada v. Canada (Minister of Finance)*, the Supreme Court of Canada held that courts should exercise their discretion to grant sealing orders where:

(1) the order is necessary to prevent a serious risk to an important interest, including a commercial interest, because reasonable alternative measures will not prevent the risk; and

(2) the salutary effects of the order outweigh its deleterious effects, including the effects on the right of free expression, which includes the public interest in open and accessible court proceedings.

[2002] S.C.J. No. 42 at para. 53 (S.C.C.).

[82] In the insolvency context, courts have applied this test and authorized sealing orders over confidential or commercially sensitive documents to protect the interests of debtors and other stakeholders, *Re Stelco Inc.*, [2006] O.J. No. 275 at paras. 2-5 (S.C.J. [Commercial List]); *Re Nortel Networks Corp.*, *supra*.

[83] It would be detrimental to the operations of Danier to disclose the identity of the individuals who will be receiving the KERP payments as this may result in other employees requesting such payments or feeling underappreciated. Further, the KERP evidence involves matters of a private, personal nature.

[84] The offer summary contains highly sensitive commercial information about Danier, the business and what some parties, confidentially, were willing to bid for Danier's assets. Disclosure of this information could undermine the integrity of the SISP. The disclosure of the offer summary prior to the completion of a final transaction under the SISP would pose a serious risk to the SISP in the event that the transaction does not close. Disclosure prior to the completion of a SISP would jeopardize value-maximizing dealings with any future prospective purchasers or liquidators of Danier's assets. There is a public interest in maximizing recovery in an insolvency that goes beyond each individual case.

[85] The sealing order is necessary to protect the important commercial interests of Danier and other stakeholders. This salutary effect greatly outweighs the deleterious effects of not sealing the KERPs and the offer summary, namely the lack of immediate public access to a limited number of documents filed in these proceedings.

[86] As a result, the *Sierra Club* test for a sealing order has been met. The material about the KERP and the offer summary shall not form part of the public record pending completion of these proposal proceedings.

Penny J.

Date: February 10, 2016

Tab 6

2004 CarswellOnt 2397
Ontario Superior Court of Justice [Commercial List]

Ivaco Inc., Re

2004 CarswellOnt 2397, [2004] O.J. No. 2483, [2004] O.T.C. 499, 131 A.C.W.S. (3d) 802, 3 C.B.R. (5th) 33

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT
OF IVACO INC. AND THE APPLICANTS LISTED IN SCHEDULE "A"

Cumming J.

Heard: June 9, 2004
Judgment: June 10, 2004
Docket: 03-CL-5145

Counsel: M.P. Gottlieb for Applicants
Michael E. Barrack, Geoff R. Hall for QIT
E. Lamek for National Bank of Canada
Peter Howard for Monitor, Ernst & Young Inc.
D.V. MacDonald for Bank of Nova Scotia
J.T. Porter for UBS
Ken Rosenberg for United Steel Workers of Canada

Subject: Insolvency

Headnote

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Arrangements — Approval by court — Miscellaneous issues

Company began proceedings under Companies' Creditors Arrangement Act — Company sought directions on possible sale proposal — Corporate restructuring officer to be part of sales process — Parties agreed that monitor could observe negotiations between QIT and bidders, and that disclosure be made of supply agreement between QIT and company — Corporate restructuring officer was required to understand all aspects of possible sale.

Table of Authorities

Statutes considered:

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

RULING regarding arrangement under *Companies' Creditors Arrangement Act*.

***Cumming J.*:**

The Motion

1 The moving party Applicants, Ivaco Rolling Mills Limited Partnership, comprising some eight affiliated corporations ("IRM"), seek directions from the Court in respect of the sales process for its business under the *Companies' Creditors Arrangement Act* ("*CCAA*"). The motion raises an important issue relating to the respective roles of the Monitor and Chief Restructuring Officer in that process. The Court provided a decision at the conclusion of the hearing, with reasons to follow.

Background

2 IRM is engaged in the steel manufacturing and processing business in Canada. QIT-Fer Et Titane Inc. ("QIT") is a major supplier to IRM of steel billets pursuant to a long-standing supply agreement. QIT is also a major unsecured creditor of IRM, being owed some $62 million.

3 The Applicants obtained an Initial Order under the *CCAA* September 16, 2003. A Chief Restructuring Officer ("CRO") was appointed October 24, 2003.

4 On December 11, 2003 this Court authorized IRM to pursue a dual-track restructuring process: one track is a stand-alone restructuring plan; the second track is the pursuit of a sales process.

5 The Monitor, the CRO and the unsecured creditors of IRM have a concern that QIT seeks a way whereby it will be paid the monies owing to it by IRM outside the parameter of the *CCAA* proceeding. The record gives some force to this concern.

6 A Court Order dated March 22, 2004 authorized a limited number of prospective purchasers to submit offers for the assets of one or more of the Applicants. Some four bidders have now submitted proposals in this regard. Understandably, it is a condition of the proposals that the bidders be able to satisfy themselves as to the nature and status of the historical and existing relationship between QIT and IRM and the nature of any relationship for the future between a buyer of IRM's business and QIT.

7 The concern that has been raised by the Monitor, CRO and a number of IRM's creditors is that QIT may seek to enter into a relationship with a bidder whereby QIT could achieve some recovery of IRM's pre-filing debt of $62 million at the expense of other unsecured creditors.

8 Any purchaser of IRM requires a supply contract with QIT as there are no apparent competitors for its product sold to IRM. The concern is that QIT could insist upon a supply arrangement with the bidder at an unreasonably high price with the bidder offering an unreasonably low price for the assets of IRM. The creditors, Monitor, and the Applicants are concerned that QIT might enter into a supply arrangement with a bidder at the expense of IRM by virtue of the price for IRM's assets being lower than would otherwise be the case in a normal market transaction.

9 Meetings have been set up to take place between the bidders, the Applicants through the CRO, the Monitor and QIT with a view to determining whether any one or more bidder can achieve a supply agreement with QIT within a context of a satisfactory unconditional bid by that bidder for the assets of one or more of the Applicants.

The Issue

10 Several issues raised at the outset of the motion were settled by agreement as discussions progressed. It is not necessary to discuss these settled issues. The settled position provides that the Monitor can observe the negotiations to take place between QIT and each bidder. The settled position also provides that disclosure can be made to bidders of the existing supply agreement between IRM and QIT.

11 A single issue remained for determination by the Court at the conclusion of the hearing, being whether or not the CRO was to be part of the sales process. QIT took the position that the CRO should not be part of the process. The Applicants, the Monitor and the other major unsecured creditors all took the position that the CRO should be part of the sales process. Only QIT, supported by the United Steel Workers of Canada, took the contrary view.

12 The only support for QIT came from the United Steel Workers of Canada, being the Union representing the workers of IRM through a collective bargaining agreement. The position expressed by counsel for the Union was that the continuity of IRM's business is critical to the direct welfare of its employees and is of indirect benefit to the community at large. There is a clear public interest in the welfare of the workers. Undoubtedly, that is a correct, and important observation.

13 Thus, counsel for the Union argued further, the Court should accede to the position of QIT even though it might result in a failure to maximize the value of the IRM assets through the *CAA* proceeding. In my view, the Union's quite proper concern for the welfare of the workers cannot justify trumping the concern of creditors that they be treated fairly. Nor would it ever be in the broader notion of the public interest to allow a sales process perceived to be unfair to go forward. The public policy underlying the *CCAA* and its objectives would be undermined. Indeed, it might well be that any proposed sale would not then garner the requisite support of creditors required for approval under the *CCAA*. It might be that the business of IRM is more likely to fail, to the ultimate disadvantage of its workers, through a compromise to the integrity of the sales process. In any event, the Court could not sanction a proposed plan of compromise that was the result of an unfair process.

14 QIT professes that if the CRO takes part in the negotiations between the bidders and QIT that this will necessarily inhibit the sales process. QIT claims this will be so because bidders will be reluctant to provide confidential information to QIT, and vice-versa, while recognizing that the CRO may then use that information to enhance an alternative stand-alone restructuring plan and consequentially advise against acceptance of the bidder's proposal.

Disposition

15 There are certain fundamentals to a *CCAA* proceeding relevant to a determination of the issue at hand. First, there cannot be a sales process whereby one unsecured creditor secures a secret benefit or advantage over the other unsecured creditors. Such a result would be the equivalent of providing a preference for that creditor. Fairness to all the creditors is a prerequisite to a satisfactory sales process. Second, the sales process must be seen to be fair. That is, there must be transparency.

16 Third, the sales process is to be determined by the Court after considering the advice of the Monitor and the position of the Applicants and their creditors. The sales process is not dictated by a supplier *qua* supplier. It may be the supplier does not wish to participate in the sales process given the nature of the process. That is for the supplier to determine in its own self-interest. In the situation at hand, QIT conceivably might say that it would rather lose its supplier relationship with IRM or a successor, to its apparent significant economic detriment, than proceed in the sales process.

17 The CRO's attendance and participation in the sales process is critical because he is the independent party who must understand all the various bids and weigh each against the possibility of a stand-alone restructuring. He must ultimately make recommendations that engender confidence as being advanced on the best information and advice possible. The CRO is an active part of the negotiations in the sales process. He is not involved as a relatively passive observer in the manner of the Monitor.

18 The sales process has been determined by the Applicants with the approval of the Court. The CRO represents the Applicants in that process. The intended sales process is one of trilateral negotiations. If QIT, IRM or any bidder wishes to discontinue such negotiations at any time that is, of course, that party's right. It is in the obvious self-interest of IRM, QIT, and any bidder to maintain the existing QIT to IRM (or successor) supply relationship. It would seem to be a win — win — win situation to come to a tripartite agreement. While no one can be ordered to enter into any new agreement every participant is required to engage in a sales process that is fair and is seen to be fair. The CRO is involved with the purpose of achieving the best result for the Applicants and a result which will be approved by the requisite number of creditors.

19 Turning to the instant situation, there are a number of Applicants with different unsecured creditors for different Applicants. It is necessary that any negotiated sale (or restructuring) take into account such complexities so that fairness is achieved for all the creditors (and is seen to be achieved.)

20 QIT proposed that the CRO would be excluded from the negotiations unless his presence was requested by either a bidder or by QIT. I disagree. In my view, the CRO has the right to attend and participate throughout the entirety of the negotiations in

the sales process. In the event that a discrete issue arises in the context of a particular bidder's negotiations with QIT, such that there is disagreement as to whether the Monitor or CRO should be absent, then the further direction of the Court can be sought in the context of that specific issue. This will allow for QIT's expressed concerns for bidders in the negotiation process to be taken into account, should this be necessary. It is noted incidentally that no bidder has come forward in the hearing at hand to support QIT in respect of its expressed concerns about the sales process.

21 Absent some compelling, exceptional factor to the contrary (not seen here), in my view, the Court should accept an applicant's proposed sales process under the *CCAA*, when it has been recommended by the Monitor and is supported by the disinterested major creditors. The Court has the discretion to stipulate a variation to such a proposed sales process plan. However, the exercising of such discretion would seem appropriate in only very exceptional circumstances.

22 An Order will issue in the form attached hereto as Annex "A". There are no costs granted to any party.

Order accordingly.

ANNEX — "A"

Court File No. 03-CL-5145

ONTARIO SUPERIOR COURT OF JUSTICE COMMERCIAL LIST

THE HONOURABLE MR. JUSTICE CUMMING

WEDNESDAY, THE 9th DAY OF JUNE, 2004

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF IVACO INC. AND THE APPLICANTS LISTED IN SCHEDULE "A"

ORDER

THIS MOTION, made by the Applicants for directions with respect to the sales process in respect of discussions involving QIT Fer et Titane Inc. ("QIT"), was heard this day at 393 University, Toronto.

ON READING the Notice of Motion, the Tenth Report of the Monitor, Ernst & Young Inc., the Affidavit of Randall C. Benson, the Affidavit of Gary A. O'Brien, and the Supplementary Affidavit of Randall C. Benson, and on hearing the submissions of counsel for the Applicants, the Monitor, QIT, the Informal Committee of Noteholders, the United Steelworkers of America, the Bank of Nova Scotia, the National Bank of Canada and UBS Securities LLC:

1. THIS COURT ORDERS that the time for service of the Notice of Motion and the Motion Record herein is abridged so that the motion is properly returnable today, and that any requirement for service of the Notice of Motion and of the Motion Record upon any party not served is dispensed with.

2. THIS COURT ORDERS that the sales process in respect of discussions involving QIT shall be governed by the following procedure:

(a) QIT shall have seven days from the date of this Order to meet with the bidders who have submitted final proposals in the second round of the sales process authorized by order of this court dated March 22, 2004. The Monitor and CRO shall have the right to attend and participate in all such meetings. At the conclusion of the seven day period, QIT shall inform the Monitor of those bidders with whom it is prepared to conduct further negotiations. After considering the views of QIT and the Applicants, the Monitor shall identify to the Applicants and QIT the bidders with whom further negotiations shall occur (the "Bidders"). If either QIT or the Applicants disagree with the Monitor then they may apply to the court for directions.

(b) After the Bidders have been identified, QIT shall disclose relevant portions of the long-term supply agreement dated April 15, 1999 between QIT and Ivaco Rolling Mills Limited Partnership ("IRM") which QIT claims has been terminated and which the Applicants claim has not been terminated (the "Agreement") to the Bidders, under appropriate confidentiality arrangements. QIT and the Monitor shall have discussions to determine what portions of the Agreement are relevant and to determine appropriate confidentiality arrangements. If they cannot agree, they shall seek further directions from the court. Further, if the Applicants do not agree with the determination of QIT and the Monitor as to what portions of the Agreement are relevant, they shall be at liberty to apply to the court for further directions regarding the disclosure of the Agreement. This order shall be without prejudice to the Applicants' position that the Agreement is not confidential and that it may disclose the entire Agreement.

(c) QIT shall then undertake negotiations with the Bidders. The Monitor and CRO shall be entitled to attend and participate in these negotiations so as to be in a position to report to the court on the outcome of them. No other parties shall participate in the negotiations, except that at the request of either QIT or a Bidder technical personnel from the Applicants will be entitled to participate in order to give necessary technical assistance. If the parties cannot agree on the appropriate participation of additional persons they shall seek further directions from the court. At the request of QIT and a Bidder, the Monitor may in its discretion absent itself from parts of negotiations which it considers best to proceed privately. If the Monitor refuses such request, QIT or the Bidder may apply to the court for directions. At the request of QIT or a Bidder, the CRO may in his discretion absent himself from parts of negotiations which he considers best to proceed privately. If the CRO refuses such request, QIT or the Bidder may apply to the court for directions.

(d) The negotiations and meetings referred to shall be conducted under appropriate confidentiality arrangements.

SCHEDULE — "A"

APPLICANTS FILING FOR CCAA

1. Ivaco Inc.

2. Ivaco Rolling Mills Inc.

3. Ifastgroupe Inc.

4. IFC (Fasteners) Inc.

5. Ifastgroupe Realty Inc.

6. Docap (1985) Corporation

7. Florida Sub One Holdings, Inc.

8. 3632610 Canada Inc.

Tab 7

2009 CarswellOnt 4467
Ontario Superior Court of Justice [Commercial List]

Nortel Networks Corp., Re

2009 CarswellOnt 4467, [2009] O.J. No. 3169, 179 A.C.W.S. (3d) 265, 55 C.B.R. (5th) 229

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

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

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

Morawetz J.

Heard: June 29, 2009
Written reasons: July 23, 2009
Docket: 09-CL-7950

Counsel: Derrick Tay, Jennifer Stam for Nortel Networks Corporation, et al
Lyndon Barnes, Adam Hirsh for Board of Directors of Nortel Networks Corporation, Nortel Networks Limited
J. Carfagnini, J. Pasquariello for Monitor, Ernst & Young Inc.
M. Starnino for Superintendent of Financial Services, Administrator of PBGF
S. Philpott for Former Employees
K. Zych for Noteholders
Pamela Huff, Craig Thorburn for MatlinPatterson Global Advisors LLC, MatlinPatterson Global Opportunities Partners III L.P., Matlin Patterson Opportunities Partners (Cayman) III L.P.
David Ward for UK Pension Protection Fund
Leanne Williams for Flextronics Inc.
Alex MacFarlane for Official Committee of Unsecured Creditors
Arthur O. Jacques, Tom McRae for Felske & Sylvain (de facto Continuing Employees' Committee)
Robin B. Schwill, Matthew P. Gottlieb for Nortel Networks UK Limited
A. Kauffman for Export Development Canada
D. Ullman for Verizon Communications Inc.
G. Benchetrit for IBM

Subject: Insolvency; Estates and Trusts

Headnote

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Miscellaneous issues

Telecommunication company entered protection under Companies' Creditors Arrangement Act ("Act") — Company decided to pursue "going concern" sales for various business units — Company entered into sale agreement with respect to assets in Code Division Multiple Access business and Long-Term Evolution Access assets — Company was pursuing sale of its other business units — Company brought motion for approval of bidding procedures and asset sale agreement — Motion granted — Court has jurisdiction to authorize sales process under Act in absence of formal plan of compromise

or arrangement and creditor vote — Sale by company which preserved its business as going concern was consistent with objectives of Act — Unless sale was undertaken at this time, long-term viability of business would be in jeopardy.

Bankruptcy and insolvency --- Administration of estate — Sale of assets — Jurisdiction of court to approve sale

Telecommunication company entered protection under Companies' Creditors Arrangement Act ("Act") — Company decided to pursue "going concern" sales for various business units — Company entered into sale agreement with respect to assets in Code Division Multiple Access business and Long-Term Evolution Access assets — Company was pursuing sale of its other business units — Company brought motion for approval of bidding procedures and asset sale agreement — Motion granted — Court has jurisdiction to authorize sales process under Act in absence of formal plan of compromise or arrangement and creditor vote — Sale by company which preserved its business as going concern was consistent with objectives of Act — Unless sale was undertaken at this time, long-term viability of business would be in jeopardy.

Table of Authorities

Cases considered by *Morawetz J.*:

Asset Engineering LP v. Forest & Marine Financial Ltd. Partnership (2009), 2009 BCCA 319, 2009 CarswellBC 1738 (B.C. C.A.) — followed

ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp. (2008), 2008 ONCA 587, 2008 CarswellOnt 4811, (sub nom. *Metcalfe & Mansfield Alternative Investments II Corp., Re)* 240 O.A.C. 245, (sub nom. *Metcalfe & Mansfield Alternative Investments II Corp., Re)* 296 D.L.R. (4th) 135, (sub nom. *Metcalfe & Mansfield Alternative Investments II Corp., Re)* 92 O.R. (3d) 513, 45 C.B.R. (5th) 163, 47 B.L.R. (4th) 123 (Ont. C.A.) — considered

ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp. (2008), 2008 CarswellOnt 5432, 2008 CarswellOnt 5433 (S.C.C.) — referred to

Boutiques San Francisco Inc., Re (2004), 2004 CarswellQue 10918, 7 C.B.R. (5th) 189 (C.S. Que.) — referred to

Calpine Canada Energy Ltd., Re (2007), 2007 CarswellAlta 1050, 2007 ABQB 504, 35 C.B.R. (5th) 1, 415 A.R. 196, 33 B.L.R. (4th) 68 (Alta. Q.B.) — referred to

Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re (1998), 1998 CarswellOnt 3346, 5 C.B.R. (4th) 299, 72 O.T.C. 99 (Ont. Gen. Div. [Commercial List]) — considered

Caterpillar Financial Services Ltd. v. Hard-Rock Paving Co. (2008), 2008 CarswellOnt 4046, 45 C.B.R. (5th) 87 (Ont. S.C.J.) — referred to

Cliffs Over Maple Bay Investments Ltd. v. Fisgard Capital Corp. (2008), 2008 BCCA 327, 2008 CarswellBC 1758, 83 B.C.L.R. (4th) 214, 296 D.L.R. (4th) 577, 434 W.A.C. 187, 258 B.C.A.C. 187, 46 C.B.R. (5th) 7, [2008] 10 W.W.R. 575 (B.C. C.A.) — distinguished

Consumers Packaging Inc., Re (2001), 150 O.A.C. 384, 27 C.B.R. (4th) 197, 2001 CarswellOnt 3482, 12 C.P.C. (5th) 208 (Ont. C.A.) — considered

Lehndorff General Partner Ltd., Re (1993), 17 C.B.R. (3d) 24, 9 B.L.R. (2d) 275, 1993 CarswellOnt 183 (Ont. Gen. Div. [Commercial List]) — referred to

PSINET Ltd., Re (2001), 28 C.B.R. (4th) 95, 2001 CarswellOnt 3405 (Ont. S.C.J. [Commercial List]) — considered

Residential Warranty Co. of Canada Inc., Re (2006), 2006 ABQB 236, 2006 CarswellAlta 383, (sub nom. *Residential Warranty Co. of Canada Inc. (Bankrupt), Re)* 393 A.R. 340, 62 Alta. L.R. (4th) 168, 21 C.B.R. (5th) 57 (Alta. Q.B.) — referred to

Royal Bank v. Soundair Corp. (1991), 7 C.B.R. (3d) 1, 83 D.L.R. (4th) 76, 46 O.A.C. 321, 4 O.R. (3d) 1, 1991 CarswellOnt 205 (Ont. C.A.) — considered

Stelco Inc., Re (2004), 2004 CarswellOnt 4084, 6 C.B.R. (5th) 316 (Ont. S.C.J. [Commercial List]) — referred to

Tiger Brand Knitting Co., Re (2005), 2005 CarswellOnt 1240, 9 C.B.R. (5th) 315 (Ont. S.C.J.) — referred to

Winnipeg Motor Express Inc., Re (2008), 2008 CarswellMan 560, 2008 MBQB 297, 49 C.B.R. (5th) 302 (Man. Q.B.) — referred to

Statutes considered:

Bankruptcy Code, 11 U.S.C.
s. 363 — referred to

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

s. 11 — referred to

s. 11(4) — considered

MOTION by company for approval of bidding procedures for sale of business and asset sale agreement.

***Morawetz J.*:**

Introduction

1 On June 29, 2009, I granted the motion of the Applicants and approved the bidding procedures (the "Bidding Procedures") described in the affidavit of Mr. Riedel sworn June 23, 2009 (the "Riedel Affidavit") and the Fourteenth Report of Ernst & Young, Inc., in its capacity as Monitor (the "Monitor") (the "Fourteenth Report"). The order was granted immediately after His Honour Judge Gross of the United States Bankruptcy Court for the District of Delaware (the "U.S. Court") approved the Bidding Procedures in the Chapter 11 proceedings.

2 I also approved the Asset Sale Agreement dated as of June 19, 2009 (the "Sale Agreement") among Nokia Siemens Networks B.V. ("Nokia Siemens Networks" or the "Purchaser"), as buyer, and Nortel Networks Corporation ("NNC"), Nortel Networks Limited ("NNL"), Nortel Networks, Inc. ("NNI") and certain of their affiliates, as vendors (collectively the "Sellers") in the form attached as Appendix "A" to the Fourteenth Report and I also approved and accepted the Sale Agreement for the purposes of conducting the "stalking horse" bidding process in accordance with the Bidding Procedures including, the Break-Up Fee and the Expense Reimbursement (as both terms are defined in the Sale Agreement).

3 An order was also granted sealing confidential Appendix "B" to the Fourteenth Report containing the schedules and exhibits to the Sale Agreement pending further order of this court.

4 The following are my reasons for granting these orders.

5 The hearing on June 29, 2009 (the "Joint Hearing") was conducted by way of video conference with a similar motion being heard by the U.S. Court. His Honor Judge Gross presided over the hearing in the U.S. Court. The Joint Hearing was conducted in accordance with the provisions of the Cross-Border Protocol, which had previously been approved by both the U.S. Court and this court.

6 The Sale Agreement relates to the Code Division Multiple Access ("CMDA") business Long-Term Evolution ("LTE") Access assets.

7 The Sale Agreement is not insignificant. The Monitor reports that revenues from CDMA comprised over 21% of Nortel's 2008 revenue. The CDMA business employs approximately 3,100 people (approximately 500 in Canada) and the LTE business employs approximately 1,000 people (approximately 500 in Canada). The purchase price under the Sale Agreement is $650 million.

Background

8 The Applicants were granted CCAA protection on January 14, 2009. Insolvency proceedings have also been commenced in the United States, the United Kingdom, Israel and France.

9 At the time the proceedings were commenced, Nortel's business operated through 143 subsidiaries, with approximately 30,000 employees globally. As of January 2009, Nortel employed approximately 6,000 people in Canada alone.

10 The stated purpose of Nortel's filing under the CCAA was to stabilize the Nortel business to maximize the chances of preserving all or a portion of the enterprise. The Monitor reported that a thorough strategic review of the company's assets and operations would have to be undertaken in consultation with various stakeholder groups.

11 In April 2009, the Monitor updated the court and noted that various restructuring alternatives were being considered.

12 On June 19, 2009, Nortel announced that it had entered into the Sale Agreement with respect to its assets in its CMDA business and LTE Access assets (collectively, the "Business") and that it was pursuing the sale of its other business units. Mr. Riedel in his affidavit states that Nortel has spent many months considering various restructuring alternatives before determining in its business judgment to pursue "going concern" sales for Nortel's various business units.

13 In deciding to pursue specific sales processes, Mr. Riedel also stated that Nortel's management considered:

(a) the impact of the filings on Nortel's various businesses, including deterioration in sales; and

(b) the best way to maximize the value of its operations, to preserve jobs and to continue businesses in Canada and the U.S.

14 Mr. Riedel notes that while the Business possesses significant value, Nortel was faced with the reality that:

(a) the Business operates in a highly competitive environment;

(b) full value cannot be realized by continuing to operate the Business through a restructuring; and

(c) in the absence of continued investment, the long-term viability of the Business would be put into jeopardy.

15 Mr. Riedel concluded that the proposed process for the sale of the Business pursuant to an auction process provided the best way to preserve the Business as a going concern and to maximize value and preserve the jobs of Nortel employees.

16 In addition to the assets covered by the Sale Agreement, certain liabilities are to be assumed by the Purchaser. This issue is covered in a comprehensive manner at paragraph 34 of the Fourteenth Report. Certain liabilities to employees are included on this list. The assumption of these liabilities is consistent with the provisions of the Sale Agreement that requires the Purchaser to extend written offers of employment to at least 2,500 employees in the Business.

17 The Monitor also reports that given that certain of the U.S. Debtors are parties to the Sale Agreement and given the desire to maximize value for the benefit of stakeholders, Nortel determined and it has agreed with the Purchaser that the Sale Agreement is subject to higher or better offers being obtained pursuant to a sale process under s. 363 of the U.S. Bankruptcy Code and that the Sale Agreement shall serve as a "stalking horse" bid pursuant to that process.

18 The Bidding Procedures provide that all bids must be received by the Seller by no later than July 21, 2009 and that the Sellers will conduct an auction of the purchased assets on July 24, 2009. It is anticipated that Nortel will ultimately seek a final sales order from the U.S. Court on or about July 28, 2009 and an approval and vesting order from this court in respect of the Sale Agreement and purchased assets on or about July 30, 2009.

19 The Monitor recognizes the expeditious nature of the sale process but the Monitor has been advised that given the nature of the Business and the consolidation occurring in the global market, there are likely to be a limited number of parties interested in acquiring the Business.

20 The Monitor also reports that Nortel has consulted with, among others, the Official Committee of Unsecured Creditors (the "UCC") and the bondholder group regarding the Bidding Procedures and is of the view that both are supportive of the timing of this sale process. (It is noted that the UCC did file a limited objection to the motion relating to certain aspects of the Bidding Procedures.)

21 Given the sale efforts made to date by Nortel, the Monitor supports the sale process outlined in the Fourteenth Report and more particularly described in the Bidding Procedures.

22 Objections to the motion were filed in the U.S. Court and this court by MatlinPatterson Global Advisors LLC, MatlinPatterson Global Opportunities Partners III L.P. and Matlin Patterson Opportunities Partners (Cayman) III L.P. (collectively, "MatlinPatterson") as well the UCC.

23 The objections were considered in the hearing before Judge Gross and, with certain limited exceptions, the objections were overruled.

Issues and Discussion

24 The threshold issue being raised on this motion by the Applicants is whether the CCAA affords this court the jurisdiction to approve a sales process in the absence of a formal plan of compromise or arrangement and a creditor vote. If the question is answered in the affirmative, the secondary issue is whether this sale should authorize the Applicants to sell the Business.

25 The Applicants submit that it is well established in the jurisprudence that this court has the jurisdiction under the CCAA to approve the sales process and that the requested order should be granted in these circumstances.

26 Counsel to the Applicants submitted a detailed factum which covered both issues.

27 Counsel to the Applicants submits that one of the purposes of the CCAA is to preserve the going concern value of debtors companies and that the court's jurisdiction extends to authorizing sale of the debtor's business, even in the absence of a plan or creditor vote.

28 The CCAA is a flexible statute and it is particularly useful in complex insolvency cases in which the court is required to balance numerous constituents and a myriad of interests.

29 The CCAA has been described as "skeletal in nature". It has also been described as a "sketch, an outline, a supporting framework for the resolution of corporate insolvencies in the public interest". *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), 45 C.B.R. (5th) 163 (Ont. C.A.) at paras. 44, 61, leave to appeal refused [2008] S.C.C.A. No. 337 (S.C.C.). ("ATB Financial").

30 The jurisprudence has identified as sources of the court's discretionary jurisdiction, *inter alia*:

> (a) the power of the court to impose terms and conditions on the granting of a stay under s. 11(4) of the CCAA;
>
> (b) the specific provision of s. 11(4) of the CCAA which provides that the court may make an order "on such terms as it may impose"; and
>
> (c) the inherent jurisdiction of the court to "fill in the gaps" of the CCAA in order to give effect to its objects. *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (1998), 5 C.B.R. (4th) 299 (Ont. Gen. Div. [Commercial List]) at para. 43; *PSINET Ltd., Re* (2001), 28 C.B.R. (4th) 95 (Ont. S.C.J. [Commercial List]) at para. 5, *ATB Financial*, *supra*, at paras. 43-52.

31 However, counsel to the Applicants acknowledges that the discretionary authority of the court under s. 11 must be informed by the purpose of the CCAA.

> Its exercise must be guided by the scheme and object of the Act and by the legal principles that govern corporate law issues. *Re Stelco Inc.* (2005), 9 C.B.R. (5th) 135 (Ont. C.A.) at para. 44.

32 In support of the court's jurisdiction to grant the order sought in this case, counsel to the Applicants submits that Nortel seeks to invoke the "overarching policy" of the CCAA, namely, to preserve the going concern. *Residential Warranty Co. of Canada Inc., Re* (2006), 21 C.B.R. (5th) 57 (Alta. Q.B.) at para. 78.

33 Counsel to the Applicants further submits that CCAA courts have repeatedly noted that the purpose of the CCAA is to preserve the benefit of a going concern business for all stakeholders, or "the whole economic community":

> The purpose of the CCAA is to facilitate arrangements that might avoid liquidation of the company and allow it to continue in business to the benefit of the whole economic community, including the shareholders, the creditors (both secured and unsecured) and the employees. *Citibank Canada v. Chase Manhattan Bank of Canada* (1991), 5 C.B.R. (3rd) 167 (Ont. Gen. Div.) at para. 29. *Re Consumers Packaging Inc.* (2001) 27 C.B.R. (4th) 197 (Ont. C.A.) at para. 5.

34 Counsel to the Applicants further submits that the CCAA should be given a broad and liberal interpretation to facilitate its underlying purpose, including the preservation of the going concern for the benefit of all stakeholders and further that it should not matter whether the business continues as a going concern under the debtor's stewardship or under new ownership, for as long as the business continues as a going concern, a primary goal of the CCAA will be met.

35 Counsel to the Applicants makes reference to a number of cases where courts in Ontario, in appropriate cases, have exercised their jurisdiction to approve a sale of assets, even in the absence of a plan of arrangement being tendered to stakeholders for a vote. In doing so, counsel to the Applicants submits that the courts have repeatedly recognized that they have jurisdiction under the CCAA to approve asset sales in the absence of a plan of arrangement, where such sale is in the best interests of stakeholders generally. *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re*, *supra*, *Re PSINet*, *supra*, *Consumers Packaging Inc., Re* [2001 CarswellOnt 3482 (Ont. C.A.)], *supra*, *Stelco Inc., Re* (2004), 6 C.B.R. (5th) 316 (Ont. S.C.J. [Commercial List]) at para. 1, *Tiger Brand Knitting Co., Re* (2005), 9 C.B.R. (5th) 315 (Ont. S.C.J.), *Caterpillar Financial Services Ltd. v. Hard-Rock Paving Co.* (2008), 45 C.B.R. (5th) 87 (Ont. S.C.J.) and *Lehndorff General Partner Ltd., Re* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]).

36 In *Re Consumers Packaging*, *supra*, the Court of Appeal for Ontario specifically held that a sale of a business as a going concern during a CCAA proceeding is consistent with the purposes of the CCAA:

> The sale of Consumers' Canadian glass operations as a going concern pursuant to the Owens-Illinois bid allows the preservation of Consumers' business (albeit under new ownership), and is therefore consistent with the purposes of the CCAA.
>
> ...we cannot refrain from commenting that Farley J.'s decision to approve the Owens-Illinois bid is consistent with previous decisions in Ontario and elsewhere that have emphasized the broad remedial purpose of flexibility of the CCAA and have approved the sale and disposition of assets during CCAA proceedings prior to a formal plan being tendered. *Re Consumers Packaging*, *supra*, *at paras. 5, 9.*

37 Similarly, in *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re*, *supra*, Blair J. (as he then was) expressly affirmed the court's jurisdiction to approve a sale of assets in the course of a CCAA proceeding before a plan of arrangement had been approved by creditors. *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re*, *supra*, at paras. 43, 45.

38 Similarly, in *PSINet Limited*, *supra*, the court approved a going concern sale in a CCAA proceeding where no plan was presented to creditors and a substantial portion of the debtor's Canadian assets were to be sold. Farley J. noted as follows:

> [If the sale was not approved,] there would be a liquidation scenario ensuing which would realize far less than this going concern sale (which appears to me to have involved a transparent process with appropriate exposure designed to maximize the proceeds), thus impacting upon the rest of the creditors, especially as to the unsecured, together with the material enlarging of the unsecured claims by the disruption claims of approximately 8,600 customers (who will be materially disadvantaged by an interrupted transition) plus the job losses for approximately 200 employees. *Re PSINet Limited*, *supra*, at para. 3.

39 In *Re Stelco Inc.*, *supra*, in 2004, Farley J. again addressed the issue of the feasibility of selling the operations as a going concern:

> I would observe that usually it is the creditor side which wishes to terminate CCAA proceedings and that when the creditors threaten to take action, there is a realization that a liquidation scenario will not only have a negative effect upon a CCAA applicant, but also upon its workforce. Hence, the CCAA may be employed to provide stability during a period of necessary financial and operational restructuring - and if a restructuring of the "old company" is not feasible, then there is the exploration of the feasibility of the sale of the operations/enterprise as a going concern (with continued employment) in whole or in part. *Re Stelco Inc*, *supra*, at para. 1.

40 I accept these submissions as being general statements of the law in Ontario. The value of equity in an insolvent debtor is dubious, at best, and, in my view, it follows that the determining factor should not be whether the business continues under the debtor's stewardship or under a structure that recognizes a new equity structure. An equally important factor to consider is whether the case can be made to continue the business as a going concern.

41 Counsel to the Applicants also referred to decisions from the courts in Quebec, Manitoba and Alberta which have similarly recognized the court's jurisdiction to approve a sale of assets during the course of a CCAA proceeding. *Boutiques San Francisco Inc., Re* (2004), 7 C.B.R. (5th) 189 (C.S. Que.), *Winnipeg Motor Express Inc., Re* (2008), 49 C.B.R. (5th) 302 (Man. Q.B.) at paras. 41, 44, and *Calpine Canada Energy Ltd., Re* (2007), 35 C.B.R. (5th) 1 (Alta. Q.B.) at para. 75.

42 Counsel to the Applicants also directed the court's attention to a recent decision of the British Columbia Court of Appeal which questioned whether the court should authorize the sale of substantially all of the debtor's assets where the debtor's plan "will simply propose that the net proceeds from the sale...be distributed to its creditors". In *Cliffs Over Maple Bay Investments Ltd. v. Fisgard Capital Corp.* (2008), 46 C.B.R. (5th) 7 (B.C. C.A.) ("*Cliffs Over Maple Bay*"), the court was faced with a

debtor who had no active business but who nonetheless sought to stave off its secured creditor indefinitely. The case did not involve any type of sale transaction but the Court of Appeal questioned whether a court should authorize the sale under the CCAA without requiring the matter to be voted upon by creditors.

43 In addressing this matter, it appears to me that the British Columbia Court of Appeal focussed on whether the court should grant the requested relief and not on the question of whether a CCAA court has the jurisdiction to grant the requested relief.

44 I do not disagree with the decision in *Cliffs Over Maple Bay*. However, it involved a situation where the debtor had no active business and did not have the support of its stakeholders. That is not the case with these Applicants.

45 The *Cliffs Over Maple Bay* decision has recently been the subject of further comment by the British Columbia Court of Appeal in *Asset Engineering LP v. Forest & Marine Financial Ltd. Partnership*, 2009 BCCA 319 (B.C. C.A.).

46 At paragraphs 24 - 26 of the *Forest and Marine* decision, Newbury J.A. stated:

> 24. In *Cliffs Over Maple Bay*, the debtor company was a real estate developer whose one project had failed. The company had been dormant for some time. It applied for CCAA protection but described its proposal for restructuring in vague terms that amounted essentially to a plan to "secure sufficient funds" to complete the stalled project (Para. 34). This court, per Tysoe J.A., ruled that although the Act can apply to single-project companies, its purposes are unlikely to be engaged in such instances, since mortgage priorities are fully straight forward and there will be little incentive for senior secured creditors to compromise their interests (Para. 36). Further, the Court stated, the granting of a stay under s. 11 is "not a free standing remedy that the court may grant whenever an insolvent company wishes to undertake a "restructuring"...Rather, s. 11 is ancillary to the fundamental purpose of the CCAA, and a stay of proceedings freezing the rights of creditors should only be granted in furtherance of the CCAA's fundamental purpose". That purpose has been described in *Meridian Developments Inc. v. Toronto Dominion Bank* (1984) 11 D.L.R. (4th) 576 (Alta. Q.B.):
>
> > The legislation is intended to have wide scope and allow a judge to make orders which will effectively maintain the status quo for a period while the insolvent company attempts to gain the approval of its creditors for a proposed arrangement which will enable the company to remain in operation for what is, hopefully, the future benefit of both the company and its creditors. [at 580]
>
> 25. The Court was not satisfied in *Cliffs Over Maple Bay* that the "restructuring" contemplated by the debtor would do anything other than distribute the net proceeds from the sale, winding up or liquidation of its business. The debtor had no intention of proposing a plan of arrangement, and its business would not continue following the execution of its proposal - thus it could not be said the purposes of the statute would be engaged...
>
> 26. In my view, however, the case at bar is quite different from *Cliffs Over Maple Bay*. Here, the main debtor, the Partnership, is at the centre of a complicated corporate group and carries on an active financing business that it hopes to save notwithstanding the current economic cycle. (The business itself which fills a "niche" in the market, has been carried on in one form or another since 1983.) The CCAA is appropriate for situations such as this where it is unknown whether the "restructuring" will ultimately take the form of a refinancing or will involve a reorganization of the corporate entity or entities and a true compromise of the rights of one or more parties. The "fundamental purpose" of the Act - to preserve the *status quo* while the debtor prepares a plan that will enable it to remain in business to the benefit of all concerned - will be furthered by granting a stay so that the means contemplated by the Act - a compromise or arrangement - can be developed, negotiated and voted on if necessary...

47 It seems to me that the foregoing views expressed in *Forest and Marine* are not inconsistent with the views previously expressed by the courts in Ontario. The CCAA is intended to be flexible and must be given a broad and liberal interpretation to achieve its objectives and a sale by the debtor which preserves its business as a going concern is, in my view, consistent with those objectives.

48 I therefore conclude that the court does have the jurisdiction to authorize a sale under the CCAA in the absence of a plan.

49 I now turn to a consideration of whether it is appropriate, in this case, to approve this sales process. Counsel to the Applicants submits that the court should consider the following factors in determining whether to authorize a sale under the CCAA in the absence of a plan:

(a) is a sale transaction warranted at this time?

(b) will the sale benefit the whole "economic community"?

(c) do any of the debtors' creditors have a *bona fide* reason to object to a sale of the business?

(d) is there a better viable alternative?

I accept this submission.

50 It is the position of the Applicants that Nortel's proposed sale of the Business should be approved as this decision is to the benefit of stakeholders and no creditor is prejudiced. Further, counsel submits that in the absence of a sale, the prospects for the Business are a loss of competitiveness, a loss of value and a loss of jobs.

51 Counsel to the Applicants summarized the facts in support of the argument that the Sale Transaction should be approved, namely:

(a) Nortel has been working diligently for many months on a plan to reorganize its business;

(b) in the exercise of its business judgment, Nortel has concluded that it cannot continue to operate the Business successfully within the CCAA framework;

(c) unless a sale is undertaken at this time, the long-term viability of the Business will be in jeopardy;

(d) the Sale Agreement continues the Business as a going concern, will save at least 2,500 jobs and constitutes the best and most valuable proposal for the Business;

(e) the auction process will serve to ensure Nortel receives the highest possible value for the Business;

(f) the sale of the Business at this time is in the best interests of Nortel and its stakeholders; and

(g) the value of the Business is likely to decline over time.

52 The objections of MatlinPatterson and the UCC have been considered. I am satisfied that the issues raised in these objections have been addressed in a satisfactory manner by the ruling of Judge Gross and no useful purpose would be served by adding additional comment.

53 Counsel to the Applicants also emphasize that Nortel will return to court to seek approval of the most favourable transaction to emerge from the auction process and will aim to satisfy the elements established by the court for approval as set out in *Royal Bank v. Soundair Corp.* (1991), 7 C.B.R. (3d) 1 (Ont. C.A.) at para. 16.

Disposition

54 The Applicants are part of a complicated corporate group. They carry on an active international business. I have accepted that an important factor to consider in a CCAA process is whether the case can be made to continue the business as a going concern. I am satisfied having considered the factors referenced at [49], as well as the facts summarized at [51], that the Applicants have met this test. I am therefore satisfied that this motion should be granted.

55 Accordingly, I approve the Bidding Procedures as described in the Riedel Affidavit and the Fourteenth Report of the Monitor, which procedures have been approved by the U.S. Court.

56 I am also satisfied that the Sale Agreement should be approved and further that the Sale Agreement be approved and accepted for the purposes of conducting the "stalking horse" bidding process in accordance with the Bidding Procedures including, without limitation the Break-Up Fee and the Expense Reimbursement (as both terms are defined in the Sale Agreement).

57 Further, I have also been satisfied that Appendix B to the Fourteenth Report contains information which is commercially sensitive, the dissemination of which could be detrimental to the stakeholders and, accordingly, I order that this document be sealed, pending further order of the court.

58 In approving the Bidding Procedures, I have also taken into account that the auction will be conducted prior to the sale approval motion. This process is consistent with the practice of this court.

59 Finally, it is the expectation of this court that the Monitor will continue to review ongoing issues in respect of the Bidding Procedures. The Bidding Procedures permit the Applicants to waive certain components of qualified bids without the consent of the UCC, the bondholder group and the Monitor. However, it is the expectation of this court that, if this situation arises, the Applicants will provide advance notice to the Monitor of its intention to do so.

Motion granted.

Tab 8

2004 CarswellOnt 1211
Ontario Superior Court of Justice [Commercial List]

Stelco Inc., Re

2004 CarswellOnt 1211, [2004] O.J. No. 1257, [2004] O.T.C. 284, 129 A.C.W.S. (3d) 1065, 48 C.B.R. (4th) 299

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

IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT WITH RESPECT TO STELCO INC. AND THE OTHER APPLICANTS LISTED IN SCHEDULE "A"

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

Farley J.

Heard: March 5, 2004
Judgment: March 22, 2004
Docket: 04-CL-5306

Counsel: Michael E. Barrack, James D. Gage, Geoff R. Hall for Applicants
David Jacobs, Michael McCreary for Locals, 1005, 5328, 8782 of the United Steel Workers of America
Ken Rosenberg, Lily Harmer, Rob Centa for United Steelworkers of America
Bob Thornton, Kyla Mahar for Ernst & Young Inc., Monitor of the Applicants
Kevin J. Zych for Informal Committee of Stelco Bondholders
David R. Byers for CIT
Kevin McElcheran for GE
Murray Gold, Andrew Hatnay for Retired Salaried Beneficiaries
Lewis Gottheil for CAW Canada and its Local 523
Virginie Gauthier for Fleet
H. Whiteley for CIBC
Gail Rubenstein for FSCO
Kenneth D. Kraft for EDS Canada Inc.

Subject: Insolvency

Headnote

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Application of Act

Steel company S Inc. applied for protection under Companies' Creditors Arrangement Act ("CCAA") on January 29, 2004 — Union locals moved to rescind initial order and dismiss initial application of S Inc. and its subsidiaries on ground S Inc. was not "debtor company" as defined in s. 2 of CCAA because S Inc. was not insolvent — Motion dismissed — Given time and steps involved in reorganization, condition of insolvency perforce required expanded meaning under CCAA — Union affiant stated that S Inc. will run out of funding by November 2004 — Given that November was ten months away from date of filing, S Inc. had liquidity problem — S Inc. realistically cannot expect any increase in its credit line with its lenders or access to further outside funding — S Inc. had negative equity of $647 million — On balance of probabilities, S Inc. was insolvent and therefore was "debtor company" as at date of filing and entitled to apply for CCAA protection.

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Challmie, Re (1976), 22 C.B.R. (N.S.) 78, 1976 CarswellBC 63 (B.C. S.C.) — considered

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

Davidson v. Douglas (1868), 15 Gr. 347, 1868 CarswellOnt 167 (Ont. Ch.) — considered

Diemaster Tool Inc. v. Skvortsoff (Trustee of) (1991), 3 C.B.R. (3d) 133, 1991 CarswellOnt 168 (Ont. Gen. Div.) — referred to

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Maybank Foods Inc. (Trustee of) v. Provisioners Maritimes Ltd. (1989), 92 N.S.R. (2d) 283, 75 C.B.R. (N.S.) 317, 45 B.L.R. 14, 237 A.P.R. 283, 1989 CarswellNS 27 (N.S. T.D.) — considered

Montreal Trust Co. of Canada v. Timber Lodge Ltd. (1992), 15 C.B.R. (3d) 14, *(*sub nom. *Timber Lodge Ltd. v. Montreal Trust Co. of Canada (No. 1))* 101 Nfld. & P.E.I.R. 73, *(*sub nom. *Timber Lodge Ltd. v. Montreal Trust Co. of Canada (No. 1))* 321 A.P.R. 73, 1992 CarswellPEI 13 (P.E.I. C.A.) — referred to

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s. 2(1) "insolvent person" (b) — considered

s. 2(1) "insolvent person" (c) — considered

s. 43(7) — referred to

s. 121(1) — referred to

s. 121(2) — referred to

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Generally — referred to

s. 2 "debtor company" — referred to

s. 2 "debtor company" (a) — considered

s. 2 "debtor company" (b) — considered

s. 2 "debtor company" (c) — considered

s. 2 "debtor company" (d) — considered

s. 12 — referred to

s. 12(1) "claim" — referred to

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Words and phrases considered:

debtor company

> It seems to me that the [*Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36] test of insolvency . . . which I have determined is a proper interpretation is that the [*Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3] definition of [s. 2(1)] (a), (b) or (c) of insolvent person is acceptable with the caveat that as to (a), a financially troubled corporation is insolvent if it is reasonably expected to run out of liquidity within reasonable proximity of time as compared with the time reasonably required to implement a restructuring.

MOTION by union that steel company was not "debtor company" as defined in *Companies' Creditors Arrangement Act*.

***Farley J.*:**

1 As argued this motion by Locals 1005, 5328 and 8782 United Steel Workers of America (collectively "Union") to rescind the initial order and dismiss the application of Stelco Inc. ("Stelco") and various of its subsidiaries (collectively "Sub Applicants") for access to the protection and process of the *Companies' Creditors Arrangement Act* ("CCAA") was that this access should be denied on the basis that Stelco was not a "debtor company" as defined in s. 2 of the CCAA because it was not insolvent.

2 Allow me to observe that there was a great deal of debate in the materials and submissions as to the reason(s) that Stelco found itself in with respect to what Michael Locker (indicating he was "an expert in the area of corporate restructuring and a leading steel industry analyst") swore to at paragraph 12 of his affidavit was the "current crisis":

> 12. Contending with weak operating results and resulting tight cash flow, management has deliberately chosen not to fund its employee benefits. By contrast, Dofasco and certain other steel companies have consistently funded both their employee benefit obligations as well as debt service. If Stelco's management had chosen to fund pension obligations, presumably with borrowed money, *the current crisis* and related restructuring plans would focus on debt restructuring as opposed to the reduction of employee benefits and related liabilities. [Emphasis added.]

3 For the purpose of determining whether Stelco is insolvent and therefore could be considered to be a debtor company, it matters not what the cause or who caused the financial difficulty that Stelco is in as admitted by Locker on behalf of the Union. The management of a corporation could be completely incompetent, inadvertently or advertently; the corporation could be in the grip of ruthless, hard hearted and hard nosed outside financiers; the corporation could be the innocent victim of uncaring policy of a level of government; the employees (unionized or non-unionized) could be completely incompetent, inadvertently or advertently; the relationship of labour and management could be absolutely poisonous; the corporation could be the victim of unforeseen events affecting its viability such a as a fire destroying an essential area of its plant and equipment or of rampaging dumping. One or more or all of these factors (without being exhaustive), whether or not of varying degree and whether or not in combination of some may well have been the cause of a corporation's difficulty. The point here is that Stelco's difficulty exists; the only question is whether Stelco is insolvent within the meaning of that in the "debtor company" definition of the CCAA. However, I would point out, as I did in closing, that no matter how this motion turns out, Stelco does have a problem which has to be addressed - addressed within the CCAA process if Stelco is insolvent or addressed outside that process if Stelco is determined not to be insolvent. The status quo will lead to ruination of Stelco (and its Sub Applicants) and as a result will very badly affect its stakeholder, including pensioners, employees (unionized and non-unionized), management, creditors, suppliers, customers, local and other governments and the local communities. In such situations, time is a precious commodity; it cannot be wasted; no matter how much some would like to take time outs, the clock cannot be stopped. The watchwords of the Commercial List are equally applicable in such circumstances. They are communication, cooperation and common sense. I appreciate that these cases frequently invoke emotions running high and wild; that is understandable on a human basis but it is the considered, rational approach which will solve the problem.

4 The time to determine whether a corporation is insolvent for the purpose of it being a "debtor company" and thus able to make an application to proceed under the CCAA is the date of filing, in this case January 29, 2004.

5 The Monitor did not file a report as to this question of insolvency as it properly advised that it wished to take a neutral role. I understand however, that it did provide some assistance in the preparation of Exhibit C to Hap Steven's affidavit.

6 If I determine in this motion that Stelco is not insolvent, then the initial order would be set aside. See *Montreal Trust Co. of Canada v. Timber Lodge Ltd.* (1992), 15 C.B.R. (3d) 14 (P.E.I. C.A.). The onus is on Stelco as I indicated in my January 29, 2004 endorsement.

7 S. 2 of the CCAA defines "debtor company" as:

> "debtor company" means any company that:
>
> (a) is bankrupt or insolvent;
>
> (b) has committed an act of bankruptcy within the meaning of *Bankruptcy and Insolvency Act* ["BIA"] or deemed insolvent within the meaning of the *Winding-Up and Restructuring Act*, whether or not proceedings in respect of the company have been taken under either of those Acts;
>
> (c) has made an authorized assignment against which a receiving order has been made under the *Bankruptcy and Insolvency Act*; or
>
> (d) is in the course of being wound-up under the *Winding-Up and Restructuring Act* because the company is insolvent.

8 Counsel for the Existing Stelco Lenders and the DIP Lenders posited that Stelco would be able to qualify under (b) in light of the fact that as of January 29, 2004 whether or not it was entitled to receive the CCAA protection under (a) as being insolvent, it had ceased to pay its pre-filing debts. I would merely observe as I did at the time of the hearing that I do not find this argument attractive in the least. The most that could be said for that is that such game playing would be ill advised and in my view would not be rewarded by the exercise of judicial discretion to allow such an applicant the benefit of a CCAA stay and other advantages of the procedure for if it were capriciously done where there is not reasonable need, then such ought not to be granted. However, I would point out that if a corporation did capriciously do so, then one might well expect a creditor-initiated application so as to take control of the process (including likely the ouster of management including directors who authorized such unnecessary stoppage); in such a case, while the corporation would not likely be successful in a corporation application, it is likely that a creditor application would find favour of judicial discretion.

9 This judicial discretion would be exercised in the same way generally as is the case where s. 43(7) of the BIA comes into play whereby a bankruptcy receiving order which otherwise meets the test may be refused. See *Kenwood Hills Development Inc., Re* (1995), 30 C.B.R. (3d) 44 (Ont. Bktcy.) where at p. 45 I observed:

> The discretion must be exercised judicially based on credible evidence; it should be used according to common sense and justice and in a manner which does not result in an injustice: See *Re Churchill Forest Industries (Manitoba) Ltd.* (1971), 16 C.B.R. (NS) 158 (Man. Q.B.).

10 Anderson J. in *MTM Electric Co., Re* (1982), 42 C.B.R. (N.S.) 29 (Ont. Bktcy.) at p. 30 declined to grant a bankruptcy receiving order for the eminently good sense reason that it would be counterproductive: "Having regard for the value of the enterprise and having regard to the evidence before me, I think it far from clear that a receiving order would confer a benefit on anyone." This common sense approach to the judicial exercise of discretion may be contrasted by the rather more puzzling approach in *TDM Software Systems Inc., Re* (1986), 60 C.B.R. (N.S.) 92 (Ont. S.C.).

11 The Union, supported by the International United Steel Workers of America ("International"), indicated that if certain of the obligations of Stelco were taken into account in the determination of insolvency, then a very good number of large Canadian corporations would be able to make an application under the CCAA. I am of the view that this concern can be addressed as follows. The test of insolvency is to be determined on its own merits, not on the basis that an otherwise technically insolvent corporation should not be allowed to apply. However, if a technically insolvent corporation were to apply and there was no material advantage to the corporation and its stakeholders (in other words, a pressing need to restructure), then one would expect that the court's discretion would be judicially exercised against granting CCAA protection and ancillary relief. In the case of Stelco, it is recognized, as discussed above, that it is in crisis and in need of restructuring - which restructuring, if it is

insolvent, would be best accomplished within a CCAA proceeding. Further, I am of the view that the track record of CCAA proceedings in this country demonstrates a healthy respect for the fundamental concerns of interested parties and stakeholders. I have consistently observed that much more can be achieved by negotiations outside the courtroom where there is a reasonable exchange of information, views and the exploration of possible solutions and negotiations held on a without prejudice basis than likely can be achieved by resorting to the legal combative atmosphere of the courtroom. A mutual problem requires a mutual solution. The basic interest of the CCAA is to rehabilitate insolvent corporations for the benefit of all stakeholders. To do this, the cause(s) of the insolvency must be fixed on a long term viable basis so that the corporation may be turned around. It is not achieved by positional bargaining in a tug of war between two parties, each trying for a larger slice of a defined size pie; it may be achieved by taking steps involving shorter term equitable sacrifices and implementing sensible approaches to improve productivity to ensure that the pie grows sufficiently for the long term to accommodate the reasonable needs of the parties.

12 It appears that it is a given that the Sub Applicants are in fact insolvent. The question then is whether Stelco is insolvent.

13 There was a question as to whether Stelco should be restricted to the material in its application as presented to the Court on January 29, 2004. I would observe that CCAA proceedings are not in the nature of the traditional adversarial lawsuit usually found in our courtrooms. It seems to me that it would be doing a disservice to the interest of the CCAA to artificially keep the Court in the dark on such a question. Presumably an otherwise deserving "debtor company" would not be allowed access to a continuing CCAA proceeding that it would be entitled to merely because some potential evidence were excluded for traditional adversarial technical reasons. I would point out that in such a case, there would be no prohibition against such a corporation reapplying (with the additional material) subsequently. In such a case, what would be the advantage for anyone of a "pause" before being able to proceed under the rehabilitative process under the CCAA. On a practical basis, I would note that all too often corporations will wait too long before applying, at least this was a significant problem in the early 1990s. In *Inducon Development Corp., Re* (1991), 8 C.B.R. (3d) 306 (Ont. Gen. Div.), I observed:

> Secondly, CCAA is designed to be remedial; it is not, however, designed to be preventative. CCAA should not be the *last* gasp of a dying company; it should be implemented, if it is to be implemented, at a stage prior to the death throe.

14 It seems to me that the phrase "death throe" could be reasonably replaced with "death spiral". In *Cumberland Trading Inc., Re* (1994), 23 C.B.R. (3d) 225 (Ont. Gen. Div. [Commercial List]), I went on to expand on this at p. 228:

> I would also observe that all too frequently debtors wait until virtually the last moment, the last moment, or in some cases, beyond the last moment before even beginning to think about reorganizational (and the attendant support that any successful reorganization requires from the creditors). I noted the lamentable tendency of debtors to deal with these situations as "last gasp" desperation moves in *Re Inducon Development Corp.* (1992), 8 C.B.R. (3d) 308 (Ont. Gen. Div.). To deal with matters on this basis minimizes the chances of success, even if "success" may have been available with earlier spade work.

15 I have not been able to find in the CCAA reported cases any instance where there has been an objection to a corporation availing itself of the facilities of the CCAA on the basis of whether the corporation was insolvent. Indeed, as indicated above, the major concern here has been that an applicant leaves it so late that the timetable of necessary steps may get impossibly compressed. That is not to say that there have not been objections by parties opposing the application on various other grounds. Prior to the 1992 amendments, there had to be debentures (plural) issued pursuant to a trust deed; I recall that in *Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 1 C.B.R. (3d) 101, 1 O.R. (3d) 289 (Ont. C.A.), the initial application was rejected in the morning because there had only been one debenture issued but another one was issued prior to the return to court that afternoon. This case stands for the general proposition that the CCAA should be given a large and liberal interpretation. I should note that there was in *Enterprise Capital Management Inc. v. Semi-Tech Corp.* (1999), 10 C.B.R. (4th) 133 (Ont. S.C.J. [Commercial List]) a determination that in a creditor application, the corporation was found not to be insolvent, but see below as to BIA test (c) my views as to the correctness of this decision.

16 In *Lehndorff General Partner Ltd., Re* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]) I observed at p. 32:

> One of the purposes of the CCAA is to facilitate ongoing operations of a business where its assets have a greater value as part of an integrated system than individually. The CCAA facilitates reorganization of a company where the alternative, sale of the property piecemeal, is likely to yield far less satisfaction to the creditors.

17 In *Anvil Range Mining Corp., Re* (2002), 34 C.B.R. (4th) 157 (Ont. C.A.), the court stated to the same effect:

> The second submission is that the plan is contrary to the purposes of the CCAA. Courts have recognized that the purpose of the CCAA is to enable compromises to be made for the common benefit of the creditors and the company and to keep the company alive and out of the hands of liquidators.

18 Encompassed in this is the concept of saving employment if a restructuring will result in a viable enterprise. See *Diemaster Tool Inc. v. Skvortsoff (Trustee of)* (1991), 3 C.B.R. (3d) 133 (Ont. Gen. Div.). This concept has been a continuing thread in CCAA cases in this jurisdiction stretching back for at least the past 15 years, if not before.

19 I would also note that the jurisprudence and practical application of the bankruptcy and insolvency regime in place in Canada has been constantly evolving. The early jails of what became Canada were populated to the extent of almost half their capacity by bankrupts. Rehabilitation and a fresh start for the honest but unfortunate debtor came afterwards. Most recently, the *Bankruptcy Act* was revised to the BIA in 1992 to better facilitate the rehabilitative aspect of making a proposal to creditors. At the same time, the CCAA was amended to eliminate the threshold criterion of there having to be debentures issued under a trust deed (this concept was embodied in the CCAA upon its enactment in 1933 with a view that it would only be large companies with public issues of debt securities which could apply). The size restriction was continued as there was now a threshold criterion of at least $5 million of claims against the applicant. While this restriction may appear discriminatory, it does have the practical advantage of taking into account that the costs (administrative costs including professional fees to the applicant, and indeed to the other parties who retain professionals) is a significant amount, even when viewed from the perspective of $5 million. These costs would be prohibitive in a smaller situation. Parliament was mindful of the time horizons involved in proposals under BIA where the maximum length of a proceeding including a stay is six months (including all possible extensions) whereas under CCAA, the length is in the discretion of the court judicially exercised in accordance with the facts and the circumstances of the case. Certainly sooner is better than later. However, it is fair to observe that virtually all CCAA cases which proceed go on for over six months and those with complexity frequently exceed a year.

20 Restructurings are not now limited in practical terms to corporations merely compromising their debts with their creditors in a balance sheet exercise. Rather there has been quite an emphasis recently on operational restructuring as well so that the emerging company will have the benefit of a long term viable fix, all for the benefit of stakeholders. See *Sklar-Peppler Furniture Corp. v. Bank of Nova Scotia* (1991), 8 C.B.R. (3d) 312 (Ont. Gen. Div.) at p. 314 where Borins J. states:

> The proposed plan exemplifies the policy and objectives of the Act as it proposes a regime for the court-supervised re-organization for the Applicant company intended to avoid the devastating social and economic effects of a creditor-initiated termination of its ongoing business operations and enabling the company to carry on its business in a manner in which it is intended to cause the least possible harm to the company, its creditors, its employees and former employees and the communities in which its carries on and carried on its business operations.

21 The CCAA does not define "insolvent" or "insolvency". Houlden & Morawetz, *The 2004 Annotated Bankruptcy and Insolvency Act* (Toronto, Carswell; 2003) at p. 1107 (N5) states:

> In interpreting "debtor company", reference must be had to the definition of "insolvent person" in s. 2(1) of the *Bankruptcy and Insolvency Act* . . .
>
> To be able to use the Act, a company must be bankrupt or insolvent: *Reference re Companies' Creditors Arrangement Act (Canada)*, 16 C.B.R. 1, [1934] S.C.R. 659, [1934] 4 D.L.R. 75. The company must, in its application, admit its insolvency.

22 It appears to have become fairly common practice for applicants and others when reference is made to insolvency in the context of the CCAA to refer to the definition of "insolvent person" in the BIA. That definition is as follows:

> s. 2(1) . . .
>
> "insolvent person" means a person who is not bankrupt and who resides, carries on business or has property in Canada, and whose liability to creditors provable as claims under this Act amount to one thousand dollars, and
>
> (a) who is for any reason unable to meet his obligations as they generally become due,
>
> (b) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or
>
> (c) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due.

23 Stelco acknowledges that it does not meet the test of (b); however, it does assert that it meets the test of both (a) and (c). In addition, however, Stelco also indicates that since the CCAA does not have a reference over to the BIA in relation to the (a) definition of "debtor company" as being a company that is "(a) bankrupt or insolvent", then this term of "insolvent" should be given the meaning that the overall context of the CCAA requires. See the modern rule of statutory interpretation which directs the court to take a contextual and purposive approach to the language of the provision at issue as illustrated by *Bell ExpressVu Ltd. Partnership v. Rex*, [2002] 2 S.C.R. 559 (S.C.C.) at p. 580:

> Today there is only one principle or approach, namely the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

24 I note in particular that the (b), (c) and (d) aspects of the definition of "debtor company" all refer to other statutes, including the BIA; (a) does not. S. 12 of the CCAA defines "claims" with reference over to the BIA (and otherwise refers to the BIA and the *Winding-Up and Restructuring Act*). It seems to me that there is merit in considering that the test for insolvency under the CCAA may differ somewhat from that under the BIA, so as to meet the special circumstances of the CCAA and those corporations which would apply under it. In that respect, I am mindful of the above discussion regarding the time that is usually and necessarily (in the circumstances) taken in a CCAA reorganization restructuring which is engaged in coming up with a plan of compromise and arrangement. The BIA definition would appear to have been historically focussed on the question of bankruptcy - and not reorganization of a corporation under a proposal since before 1992, secured creditors could not be forced to compromise their claims, so that in practice there were no reorganizations under the former *Bankruptcy Act* unless all secured creditors voluntarily agreed to have their secured claims compromised. The BIA definition then was essentially useful for being a pre-condition to the "end" situation of a bankruptcy petition or voluntary receiving order where the upshot would be a realization on the bankrupt's assets (not likely involving the business carried on - and certainly not by the bankrupt). Insolvency under the BIA is also important as to the Paulian action events (eg., fraudulent preferences, settlements) as to the conduct of the debtor *prior* to the bankruptcy; similarly as to the question of provincial preference legislation. Reorganization under a plan or proposal, on the contrary, is with a general objective of the applicant continuing to exist, albeit that the CCAA may also be used to have an orderly disposition of the assets and undertaking in whole or in part.

25 It seems to me that given the time and steps involved in a reorganization, and the condition of insolvency perforce requires an expanded meaning under the CCAA. Query whether the definition under the BIA is now sufficient in that light for the allowance of sufficient time to carry through with a realistically viable proposal within the maximum of six months allowed under the BIA? I think it sufficient to note that there would not be much sense in providing for a rehabilitation program of restructuring/reorganization under either statute if the entry test was that the applicant could not apply until a rather late stage of its financial difficulties with the rather automatic result that in situations of complexity of any material degree, the applicant

would not have the financial resources sufficient to carry through to hopefully a successful end. This would indeed be contrary to the renewed emphasis of Parliament on "rescues" as exhibited by the 1992 and 1997 amendments to the CCAA and the BIA.

26 Allow me now to examine whether Stelco has been successful in meeting the onus of demonstrating with credible evidence on a common sense basis that it is insolvent within the meaning required by the CCAA in regard to the interpretation of "debtor company" in the context and within the purpose of that legislation. To a similar effect, see *PWA Corp. v. Gemini Group Automated Distribution Systems Inc.* (1993), 103 D.L.R. (4th) 609 (Ont. C.A.), leave to appeal to S.C.C. dismissed [(1993), 49 C.P.R. (3d) ix (S.C.C.)] wherein it was determined that the trial judge was correct in holding that a party was not insolvent and that the statutory definition of insolvency pursuant to the BIA definition was irrelevant to determine that issue, since the agreement in question effectively provided its own definition by implication. It seems to me that the CCAA test of insolvency advocated by Stelco and which I have determined is a proper interpretation is that the BIA definition of (a), (b) or (c) of insolvent person is acceptable with the caveat that as to (a), a financially troubled corporation is insolvent if it is reasonably expected to run out of liquidity within reasonable proximity of time as compared with the time reasonably required to implement a restructuring. That is, there should be a reasonable cushion, which cushion may be adjusted and indeed become in effect an encroachment depending upon reasonable access to DIP between financing. In the present case, Stelco accepts the view of the Union's affiant, Michael Mackey of Deloitte and Touche that it will otherwise run out of funding by November 2004.

27 On that basis, allow me to determine whether Stelco is insolvent on the basis of (i) what I would refer to as the CCAA test as described immediately above, (ii) BIA test (a) or (iii) BIA test (c). In doing so, I will have to take into account the fact that Stephen, albeit a very experienced and skilled person in the field of restructurings under the CCAA, unfortunately did not appreciate that the material which was given to him in Exhibit E to his affidavit was modified by the caveats in the source material that in effect indicated that based on appraisals, the fair value of the real assets acquired was in excess of the purchase price for two of the U.S. comparators. Therefore the evidence as to these comparators is significantly weakened. In addition at Q. 175-177 in his cross examination, Stephen acknowledged that it was reasonable to assume that a purchaser would "take over some liabilities, some pension liabilities and OPEB liabilities, for workers who remain with the plant." The extent of that assumption was not explored; however, I do note that there was acknowledgement on the part of the Union that such an assumption would also have a reciprocal negative effect on the purchase price.

28 The BIA tests are disjunctive so that anyone meeting any of these tests is determined to be insolvent: see *Optical Recording Laboratories Inc., Re* (1990), 75 D.L.R. (4th) 747 (Ont. C.A.) at p. 756; *Viteway Natural Foods Ltd., Re* (1986), 63 C.B.R. (N.S.) 157 (B.C. S.C.) at p. 161. Thus, if I determine that Stelco is insolvent on *any one* of these tests, then it would be a "debtor company" entitled to apply for protection under the CCAA.

29 In my view, the Union's position that Stelco is not insolvent under BIA (a) because it has not entirely used up its cash and cash facilities (including its credit line), that is, it is not yet as of January 29, 2004 run out of liquidity conflates inappropriately the (a) test with the (b) test. The Union's view would render the (a) test necessarily as being redundant. See *R. v. Proulx*, [2000] 1 S.C.R. 61 (S.C.C.) at p. 85 for the principle that no legislative provision ought to be interpreted in a manner which would "render it mere surplusage." Indeed the plain meaning of the phrase "unable to meet his obligations as they generally become due" requires a construction of test (a) which permits the court to take a purposive assessment of a debtor's ability to meet his future obligations. See *King Petroleum Ltd., Re* (1978), 29 C.B.R. (N.S.) 76 (Ont. S.C.) where Steele J. stated at p. 80:

> With respect to cl. (a), it was argued that at the time the disputed payments were made the company was able to meet its obligations as they generally became due because no major debts were in fact due at that time. This was premised on the fact that the moneys owed to Imperial Oil were not due until 10 days after the receipt of the statements and that the statements had not then been received. I am of the opinion that this is not a proper interpretation of cl. (a). *Clause (a) speaks in the present and future tenses and not in the past.* I am of the opinion that the company was an "insolvent person" within the meaning of cl. (a) because by the very payment-out of the money in question it placed itself in a position that it was unable to meet its obligations as they would generally become due. In other words, it had placed itself in a position that it would not be able to pay the obligations that it knew it had incurred and which it knew would become due in the immediate future. [Emphasis added.]

30 *King Petroleum Ltd.* was a case involving the question in a bankruptcy scenario of whether there was a fraudulent preference during a period when the corporation was insolvent. Under those circumstances, the "immediate future" does not have the same expansive meaning that one would attribute to a time period in a restructuring forward looking situation.

31 Stephen at paragraphs 40-49 addressed the restructuring question in general and its applicability to the Stelco situation. At paragraph 41, he outlined the significant stages as follows:

> The process of restructuring under the CCAA entails a number of different stages, the most significant of which are as follows:
>
> (a) identification of the debtor's stakeholders and their interests;
>
> (b) arranging for a process of meaningful communication;
>
> (c) dealing with immediate relationship issues arising from a CCAA filing;
>
> (d) sharing information about the issues giving rise to the debtor's need to restructure;
>
> (e) developing restructuring alternatives; and
>
> (f) building a consensus around a plan of restructuring.

32 I note that January 29, 2004 is just 9-10 months away from November 2004. I accept as correct his conclusion based on his experience (and this is in accord with my own objective experience in large and complicated CCAA proceedings) that Stelco would have the liquidity problem within the time horizon indicated. In that regard, I also think it fair to observe that Stelco realistically cannot expect any increase in its credit line with its lenders or access further outside funding. To bridge the gap it must rely upon the stay to give it the uplift as to prefiling liabilities (which the Union misinterpreted as a general turnaround in its cash position without taking into account this uplift). As well, the Union was of the view that recent price increases would relieve Stelco's liquidity problems; however, the answers to undertaking in this respect indicated:

> With respect to the Business Plan, the average spot market sales price per ton was $514, and the average contract business sales price per ton was $599. The Forecast reflects an average spot market sales price per ton of $575, and average contract business sales price per ton of $611. The average spot price used in the forecast considers further announced price increases, recognizing, among other things, the timing and the extent such increases are expected to become effective. The benefit of the increase in sales prices from the Business Plan is essentially offset by the substantial increase in production costs, and in particular in raw material costs, primarily scrap and coke, as well as higher working capital levels and a higher loan balance outstanding on the CIT credit facility as of January 2004.

I accept that this is generally a cancel out or wash in all material respects.

33 I note that $145 million of cash resources had been used from January 1, 2003 to the date of filing. Use of the credit facility of $350 million had increased from $241 million on November 30, 2003 to $293 million on the date of filing. There must be a reasonable reserve of liquidity to take into account day to day, week to week or month to month variances and also provide for unforeseen circumstances such as the breakdown of a piece of vital equipment which would significantly affect production until remedied. Trade credit had been contracting as a result of appreciation by suppliers of Stelco's financial difficulties. The DIP financing of $75 million is only available if Stelco is under CCAA protection. I also note that a shut down as a result of running out of liquidity would be complicated in the case of Stelco and that even if conditions turned around more than reasonably expected, start-up costs would be heavy and quite importantly, there would be a significant erosion of the customer base (reference should be had to the Slater Hamilton plant in this regard). One does not liquidate assets which one would not sell in the ordinary course of business to thereby artificially salvage some liquidity for the purpose of the test: see *Pacific Mobile Corp., Re* (1979), 32 C.B.R. (N.S.) 209 (C.S. Que.) at p. 220. As a rough test, I note that Stelco (albeit on a consolidated basis

with all subsidiaries) running significantly behind plan in 2003 from its budget of a profit of $80 million now to a projected loss of $192 million and cash has gone from a positive $209 million to a negative $114 million.

34 Locker made the observation at paragraph 8 of his affidavit that:

> 8. Stelco has performed poorly for the past few years primarily due to an inadequate business strategy, poor utilization of assets, inefficient operations and generally weak management leadership and decision-making. This point is best supported by the fact that Stelco's local competitor, Dofasco, has generated outstanding results in the same period.

Table 1 to his affidavit would demonstrate that Dofasco has had superior profitability and cashflow performance than its "neighbour" Stelco. He went on to observe at paragraphs 36-37:

> 36. Stelco can achieve significant cost reductions through means other than cutting wages, pensions and benefits for employees and retirees. Stelco could bring its cost levels down to those of restructured U.S. mills, with the potential for lowering them below those of many U.S. mills.
>
> 37. Stelco could achieve substantial savings through productivity improvements within the mechanisms of the current collective agreements. More importantly, a major portion of this cost reduction could be achieved through constructive negotiations with the USWA in an out-of-court restructuring that does not require intervention of the courts through the vehicle of CCAA protection.

I accept his constructive comments that there is room for cost reductions and that there are substantial savings to be achieved through productivity improvements. However, I do not see anything detrimental to these discussions and negotiations by having them conducted within the umbrella of a CCAA proceeding. See my comments above regarding the CCAA in practice.

35 But I would observe and I am mystified by Locker's observations at paragraph 12 (quoted above), that Stelco should have borrowed to fund pension obligations to avoid its current financial crisis. This presumes that the borrowed funds would not constitute an obligation to be paid back as to principal and interest, but rather that it would assume the character of a cost-free "gift".

36 I note that Mackey, without the "laundry list" he indicates at paragraph 17 of his second affidavit, is unable to determine at paragraph 19 (for himself) whether Stelco was insolvent. Mackey was unable to avail himself of all available information in light of the Union's refusal to enter into a confidentiality agreement. He does not closely adhere to the BIA tests as they are defined. In the face of positive evidence about an applicant's financial position by an experienced person with expertise, it is not sufficient to displace this evidence by filing evidence which goes no further than raising questions: see *Anvil Range Mining Corp.*, *supra* at p. 162.

37 The Union referred me to one of my decisions *Standard Trustco Ltd. (Trustee of) v. Standard Trust Co.* (1993), 13 O.R. (3d) 7 (Ont. Gen. Div.) where I stated as to the MacGirr affidavit:

> The Trustee's cause of action is premised on MacGirr's opinion that STC was insolvent as at August 3, 1990 and therefore the STC common shares and promissory note received by Trustco in return for the Injection had no value at the time the Injection was made. Further, MacGirr ascribed no value to the opportunity which the Injection gave to Trustco to restore STC and salvage its thought to be existing $74 million investment. In stating his opinion MacGirr defined solvency as:
>
> (a) the ability to meet liabilities as they fall due; and
>
> (b) that assets exceed liabilities.
>
> On cross-examination MacGirr testified that in his opinion on either test STC was insolvent as at August 3, 1990 since as to (a) STC was experiencing then a negative cash flow and as to (b) the STC financial statements incorrectly reflected values. As far as (a) is concerned, I would comment that while I concur with MacGirr that at some time in the long run a

> company that is experiencing a negative cash flow will eventually not be able to meet liabilities as they fall due but that is not the test (which is a "present exercise"). On that current basis STC was meeting its liabilities on a timely basis.

38 As will be seen from that expanded quote, MacGirr gave his own definitions of insolvency which are not the same as the s. 2 BIA tests (a), (b) and (c) but only a very loose paraphrase of (a) and (c) and an omission of (b). Nor was I referred to the *King Petroleum Ltd.* or *Proulx* cases *supra*. Further, it is obvious from the context that "*sometime in the long run . . . eventually*" is not a finite time in the foreseeable future.

39 I have not given any benefit to the $313 - $363 million of improvements referred to in the affidavit of William Vaughan at paragraph 115 as those appear to be capital expenditures which will have to be accommodated within a plan of arrangement or after emergence.

40 It seems to me that if the BIA (a) test is restrictively dealt with (as per my question to Union counsel as to how far in the future should one look on a prospective basis being answered "24 hours") then Stelco would not be insolvent under that test. However, I am of the view that that would be unduly restrictive and a proper contextual and purposive interpretation to be given when it is being used for a restructuring purpose even under BIA would be to see whether there is a reasonably foreseeable (at the time of filing) expectation that there is a looming liquidity condition or crisis which will result in the applicant running out of "cash" to pay its debts as they generally become due in the future without the benefit of the say and ancillary protection and procedure by court authorization pursuant to an order. I think this is the more appropriate interpretation of BIA (a) test in the context of a reorganization or "rescue" as opposed to a threshold to bankruptcy consideration or a fraudulent preferences proceeding. On that basis, I would find Stelco insolvent from the date of filing. Even if one were not to give the latter interpretation to the BIA (a) test, clearly for the above reasons and analysis, if one looks at the meaning of "insolvent" within the context of a CCAA reorganization or rescue solely, then of necessity, the time horizon must be such that the liquidity crisis would occur in the sense of running out of "cash" but for the grant of the CCAA order. On that basis Stelco is certainly insolvent given its limited cash resources unused, its need for a cushion, its rate of cash burn recently experienced and anticipated.

41 What about the BIA (c) test which may be roughly referred to as an assets compared with obligations test. See *New Quebec Raglan Mines Ltd. v. Blok-Andersen*, [1993] O.J. No. 727 (Ont. Gen. Div. [Commercial List]) as to fair value and fair market valuation. The Union observed that there was no intention by Stelco to wind itself up or proceed with a sale of some or all of its assets and undertaking and therefore some of the liabilities which Stelco and Stephen took into account would not crystallize. However, as I discussed at the time of the hearing, the (c) test is what one might reasonably call or describe as an "artificial" or notional/hypothetical test. It presumes certain things which are in fact not necessarily contemplated to take place or to be involved. In that respect, I appreciate that it may be difficult to get one's mind around that concept and down the right avenue of that (c) test. See my views at trial in *Olympia & York Developments Ltd. (Trustee of) v. Olympia & York Realty Corp.*, [2001] O.J. No. 3394 (Ont. S.C.J. [Commercial List]) at paragraphs 13, 21 and 33; affirmed [2003] O.J. No. 5242 (Ont. C.A.). At paragraph 33, I observed in closing:

> 33 . . . They (and their expert witnesses) all had to contend with dealing with rambling and complicated facts and, in Section 100 BIA, a section which is difficult to administer when fmv [fair market value] in a notational or hypothetical market involves ignoring what would often be regarded as self evidence truths but at the same time appreciating that this notational or hypothetical market requires that the objects being sold have to have realistic true to life attributes recognized.

42 The Court of Appeal stated at paragraphs 24-25 as follows:

> 24. Nor are the appellants correct to argue that the trial judge also assumed an imprudent vendor in arriving at his conclusion about the fair market value of the OYSF note would have to know that in order to realize value from the note any purchaser would immediately put OYSF and thus OYDL itself into bankruptcy to pre-empt a subsequent triggering event in favour of EIB. While this was so, and the trial judge clearly understood it, the error in this submission is that it seeks to inject into the analysis factors subjected to the circumstances of OYDL as vendor and not intrinsic to the value of the OYSF note. The calculation of fair market value does not permit this but rather must assume an unconstrained vendor.

> 25. The Applicants further argue that the trial judge eroded in determining the fair market value of the OYSF note by reference to a transaction which was entirely speculative because it was never considered by OYDL nor would have it been since it would have resulted in OYDL's own bankruptcy. I disagree. The transaction hypothesized by the trial judge was one between a notational, willing, prudent and informed vendor and purchaser based on factors relevant to the OYSF note itself rather than the particular circumstances of OYDL as the seller of the note. This is an entirely appropriate way to determine the fair market value of the OYSF note.

43 Test (c) deems a person to be insolvent if "the aggregate of [its] property is not, at a fair valuation, sufficient, or of disposed at a fairly conducted sale under legal process would not be sufficient to enable payment of all [its] obligations, due and accruing due." The origins of this legislative test appear to be the decision of Spragge V-C in *Davidson v. Douglas* (1868), 15 Gr. 347 (Ont. Ch.) at p. 351 where he stated with respect to the solvency or insolvency of a debtor, the proper course is:

> to see and examine whether all his property, real and personal, be sufficient if presently realized for the payment of his debts, and in this view we must estimate his land, as well as his chattel property, not at what his neighbours or others may consider to be its value, but at what it would bring in the market at a forced sale, or a sale where the seller cannot await his opportunities, but must sell.

44 In *Clarkson v. Sterling* (1887), 14 O.R. 460 (Ont. C.P.) at p. 463, Rose J. indicted that the sale must be fair and reasonable, but that the determination of fairness and reasonableness would depend on the facts of each case.

45 The Union essentially relied on garnishment cases. Because of the provisions relating as to which debts may or may not be garnished, these authorities are of somewhat limited value when dealing with the test (c) question. However I would refer to one of the Union's cases *Bank of Montreal v. I.M. Krisp Foods Ltd.*, [1996] S.J. No. 655 (Sask. C.A.) where it is stated at paragraph 11:

> 11. Few phrases have been as problematic to define as "debt due or accruing due". The Shorter Oxford English Dictionary, 3rd ed. defines "accruing" as "arising in due course", but an examination of English and Canadian authority reveals that not all debts "arising in due course" are permitted to be garnisheed. (See Professor Dunlop's extensive research for his British Columbia Law Reform Commission's Report on Attachment of Debts Act, 1978 at 17 to 29 and is text Creditor-Debtor Law in Canada, 2nd ed. at 374 to 385.)

46 In *Barsi v. Farcas* (1923), [1924] 1 D.L.R. 1154 (Sask. C.A.), Lamont J.A. was cited for his statement at p. 522 of *Webb v. Stenton* (1883), 11 Q.B.D. 518 (Eng. C.A.) that: "an accruing debt, therefore, is a debt not yet actually payable, but a debt which is represented by an existing obligation."

47 Saunders J. noted in *633746 Ontario Inc. (Trustee of) v. Salvati* (1990), 79 C.B.R. (N.S.) 72 (Ont. S.C.) at p. 81 that a sale out of the ordinary course of business would have an adverse effect on that actually realized.

48 There was no suggestion by any of the parties that any of the assets and undertaking would have any enhanced value from that shown on the financial statements prepared according to GAAP.

49 In *King Petroleum Ltd.*, *supra* at p. 81 Steele J. observed:

> To consider the question of insolvency under cl. (c) I must look to the aggregate property of the company and come to a conclusion as to whether or not it would be sufficient to enable payment of all obligations due and accruing due. There are two tests to be applied: First, its fair value and, secondly, its value if disposed of at a fairly conducted sale under legal process. The balance sheet is a starting point, but the evidence relating to the fair value of the assets and what they might realize if disposed of at a fairly conducted sale under legal process must be reviewed in interpreting it. In this case, I find no difficulty in accepting the obligations shown as liabilities because they are known. I have more difficulty with respect to the assets.

50 To my view the preferable interpretation to be given to "sufficient to enable payment of all his obligations, due and accruing due" is to be determined in the context of this test as a whole. What is being put up to satisfy those obligations is the debtor's assets and undertaking *in total*; in other words, the debtor in essence is taken as having sold everything. There would be no residual assets and undertaking to pay off any obligations which would not be encompassed by the phrase "all of his obligations, due and accruing due". Surely, there cannot be "orphan" obligations which are left hanging unsatisfied. It seems to me that the intention of "due and accruing due" was to cover off all obligations of whatever nature or kind and leave nothing in limbo.

51 S. 121(1) and (2) of the BIA, which are incorporated by reference in s. 12 of the CCAA, provide in respect to provable claims:

> S. 121(1) All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.
>
> (2) The determination whether a contingent or unliquidated claim is a provable claim and the valuation of such claim shall be made in accordance with s. 135.

52 *Houlden and Morawetz 2004 Annotated supra* at p. 537 (G28(3)) indicates:

> The word "liability" is a very broad one. It includes all obligations to which the bankrupt is subject on the day on which he becomes bankrupt except for contingent and unliquidated claims which are dealt with in s. 121(2).

However contingent and unliquidated claims would be encompassed by the term "obligations".

53 In *Gardner v. Newton* (1916), 29 D.L.R. 276 (Man. K.B.), Mathers C.J.K.B. observed at p. 281 that "contingent claim, that is, a claim which may or may not ripen into a debt, according as some future event does or does not happen." See *A Debtor (No. 64 of 1992), Re*, [1993] 1 W.L.R. 264 (Eng. Ch. Div.) at p. 268 for the definition of a "liquidated sum" which is an amount which can be readily ascertained and hence by corollary an "unliquidated claim" would be one which is not easily ascertained, but will have to be valued. In *Gagnier, Re* (1950), 30 C.B.R. 74 (Ont. S.C.), there appears to be a conflation of not only the (a) test with the (c) test, but also the invocation of the judicial discretion not to grant the receiving order pursuant to a bankruptcy petition, notwithstanding that "[the judge was] unable to find the debtor is bankrupt". The debtor was able to survive the (a) test as he had the practice (accepted by all his suppliers) of providing them with post dated cheques. The (c) test was not a problem since the judge found that his assets should be valued at considerably more than his obligations. However, this case does illustrate that the application of the tests present some difficulties. These difficulties are magnified when one is dealing with something more significantly complex and a great deal larger than a haberdashery store - in the case before us, a giant corporation in which, amongst other things, is engaged in a very competitive history including competition from foreign sources which have recently restructured into more cost efficient structures, having shed certain of their obligations. As well, that is without taking into account that a sale would entail significant transaction costs. Even of greater significance would be the severance and termination payments to employees not continued by the new purchaser. Lastly, it was recognized by everyone at the hearing that Stelco's plants, especially the Hamilton-Hilton works, have extremely high environmental liabilities lurking in the woodwork. Stephen observed that these obligations would be substantial, although not quantified.

54 It is true that there are no appraisals of the plant and equipment nor of the assets and undertaking of Stelco. Given the circumstances of this case and the complexities of the market, one may realistically question whether or not the appraisals would be all that helpful or accurate.

55 I would further observe that in the notional or hypothetical exercise of a sale, then all the obligations which would be triggered by such sale would have to be taken into account.

56 All liabilities, contingent or unliquidated would have to be taken into account. See *King Petroleum Ltd.*, *supra* p. 81; *Salvati*, *supra* pp. 80-1; *Maybank Foods Inc. (Trustee of) v. Provisioners Maritimes Ltd.* (1989), 45 B.L.R. 14 (N.S. T.D.) at p. 29; *Challmie, Re* (1976), 22 C.B.R. (N.S.) 78 (B.C. S.C.), at pp. 81-2. In *Challmie* the debtor ought to have known that his guarantee was very much exposed given the perilous state of his company whose liabilities he had guaranteed. It is interesting to note what was stated in *Maybank Foods Inc. (Trustee of)*, even if it is rather patently obvious. Tidman J. said in respect of the branch of the company at p. 29:

> Mr. MacAdam argues also that the $4.8 million employees' severance obligation was not a liability on January 20, 1986. The *Bankruptcy Act* includes as obligations both those due and accruing due. Although the employees' severance obligation was not due and payable on January 20, 1986 it was an obligation "accruing due". The Toronto facility had experienced severe financial difficulties for some time; in fact, it was the major, if not the sole cause, of Maybank's financial difficulties. I believe it is reasonable to conclude that a reasonably astute perspective buyer of the company has a going concern would have considered that obligation on January 20, 1986 and that it would have substantially reduced the price offered by that perspective buyer. Therefore that obligation must be considered as an obligation of the company on January 20, 1986.

57 With the greatest of respect for my colleague, I disagree with the conclusion of Ground J. in *Enterprise Capital Management Inc.*, *supra* as to the approach to be taken to "due and accruing due" when he observed at pp. 139-140:

> It therefore becomes necessary to determine whether the principle amount of the Notes constitutes an obligation "due or accruing due" as of the date of this application.
>
> There is a paucity of helpful authority on the meaning of "accruing due" for purposes of a definition of insolvency. Historically, in 1933, in *P. Lyall & Sons Construction Co. v. Baker*, [1933] O.R. 286 (Ont. C.A.), the Ontario Court of Appeal, in determining a question of set-off under the *Dominion Winding-Up Act* had to determine whether the amount claimed as set-off was a debt due or accruing due to the company in liquidation for purposes of that Act. Marsten J. at pp. 292-293 quoted from Moss J.A. in *Mail Printing Co. v. Clarkson* (1898), 25 O.R. 1 (Ont. C.A.) at p. 8:
>
> > A debt is defined to be a sum of money which is certainly, and at all event, payable without regard to the fact whether it be payable now or at a future time. And an accruing debt is a debt not yet actually payable, but a debt which is represented by an existing obligation: Per Lindley L.J. in *Webb v. Stenton* (1883), 11 Q.D.D. at p. 529.
>
> Whatever relevance such definition may have had for purposes of dealing with claims by and against companies in liquidation under the old winding-up legislation, it is apparent to me that it should not be applied to definitions of insolvency. To include every debt payable at some future date in "accruing due" for the purposes of insolvency tests would render numerous corporations, with long term debt due over a period of years in the future and anticipated to be paid out of future income, "insolvent" for the purposes of the BIA and therefore the CCAA. For the same reason, I do not accept the statement quoted in the Enterprise factum from the decision of the Bankruptcy Court for the Southern District of New York in *Centennial Textiles Inc., Re*, 220 B.R. 165 (U.S.N.Y.D.C. 1998) that "if the present saleable value of assets are less than the amount required to pay existing debt as they mature, the debtor is insolvent". In my view, the obligations, which are to be measured against the fair valuation of a company's property as being obligations due and accruing due, must be limited to obligations currently payable or properly chargeable to the accounting period during which the test is being applied as, for example, a sinking fund payment due within the current year. Black's Law Dictionary defines "accrued liability" as "an obligation or debt which is properly chargeable in a given accounting period, but which is not yet paid or payable". The principal amount of the Notes is neither due nor accruing due in this sense.

58 There appears to be some confusion in this analysis as to "debts" and "obligations", the latter being much broader than debts. Please see above as to my views concerning the floodgates argument under the BIA and CCAA being addressed by judicially exercised discretion even if "otherwise warranted" applications were made. I pause to note that an insolvency test under general corporate litigation need not be and likely is not identical, or indeed similar to that under these insolvency statutes. As well, it is curious to note that the cut off date is the end of the current fiscal period which could have radically different

results if there were a calendar fiscal year and the application was variously made in the first week of January, mid-summer or the last day of December. Lastly, see above and below as to my views concerning the proper interpretation of this question of "accruing due".

59 It seems to me that the phrase "accruing due" has been interpreted by the courts as broadly identifying obligations that will "become due". See *Viteway Natural Foods Ltd.* below at pp. 163-4 - at least at some point in the future. Again, I would refer to my conclusion above that *every obligation* of the corporation in the hypothetical or notional sale must be treated as "accruing due" to avoid orphan obligations. In that context, it matters not that a wind-up pension liability may be discharged over 15 years; in a test (c) situation, it is crystallized on the date of the test. See *Optical Recording Laboratories Inc. supra* at pp. 756-7; *Viteway Natural Foods Ltd., Re* (1986), 63 C.B.R. (N.S.) 157 (B.C. S.C.) at pp. 164-63-4; *Consolidated Seed Exports Ltd., Re* (1986), 62 C.B.R. (N.S.) 156 (B.C. S.C.) at p. 163. In *Consolidated Seed Exports Ltd.*, Spencer J. at pp. 162-3 stated:

> In my opinion, a futures broker is not in that special position. The third definition of "insolvency" may apply to a futures trader at any time even though he has open long positions in the market. Even though Consolidated's long positions were not required to be closed on 10th December, the chance that they might show a profit by March 1981 or even on the following day and thus wipe out Consolidated's cash deficit cannot save it from a condition of insolvency on that day. The circumstances fit precisely within the third definition; if all Consolidated's assets had been sold on that day at a fair value, the proceeds would not have covered its obligations due and accruing due, including its obligations to pay in March 1981 for its long positions in rapeseed. The market prices from day to day establish a fair valuation. . . .
>
> The contract to buy grain at a fixed price at a future time imposes a present obligation upon a trader taking a long position in the futures market to take delivery in exchange for payment at that future time. It is true that in the practice of the market, that obligation is nearly always washed out by buying an offsetting short contract, but until that is done the obligation stands. The trader does not know who will eventually be on the opposite side of his transaction if it is not offset but all transactions are treated as if the clearing house is on the other side. It is a present obligation due at a future time. It is therefore an obligation accruing due within the meaning of the third definition of "insolvency".

60 The possibility of an expectancy of future profits or a change in the market is not sufficient; *Consolidated Seed Exports Ltd.* at p. 162 emphasizes that the test is to be done on that day, the day of filing in the case of an application for reorganization.

61 I see no objection to using Exhibit C to Stephen's affidavit as an aid to review the balance sheet approach to test (c). While Stephen may not have known who prepared Exhibit C, he addressed each of its components in the text of his affidavit and as such he could have mechanically prepared the exhibit himself. He was comfortable with and agreed with each of its components. Stelco's factum at paragraphs 70-1 submits as follows:

> 70. In Exhibit C to his Affidavit, Mr. Stephen addresses a variety of adjustments to the Shareholder's Equity of Stelco necessary to reflect the values of assets and liabilities as would be required to determine whether Stelco met the test of insolvency under Clause C. In cross examination of both Mr. Vaughan and Mr. Stephen only one of these adjustments was challenged - the "Possible Reductions in Capital Assets."
>
> 71. The basis of the challenge was that the comparative sales analysis was flawed. In the submission of Stelco, none of these challenges has any merit. Even if the entire adjustment relating to the value in capital assets is ignored, the remaining adjustments leave Stelco with assets worth over $600 million less than the value of its obligations due and accruing due. This fundamental fact is not challenged.

62 Stelco went on at paragraphs 74-5 of its factum to submit:

> 74. The values relied upon by Mr. Stephen if anything, understate the extent of Stelco's insolvency. As Mr. Stephen has stated, and no one has challenged by affidavit evidence or on cross examination, in a fairly conducted sale under legal process, the value of Stelco's working capital and other assets would be further impaired by: (i) increased environmental liabilities not reflected on the financial statements, (ii) increased pension deficiencies that would be

> generated on a wind up of the pension plans, (iii) severance and termination claims and (iv) substantial liquidation costs that would be incurred in connection with such a sale.
>
> 75. No one on behalf of the USWA has presented any evidence that the capital assets of Stelco are in excess of book value on a stand alone basis. Certainly no one has suggested that these assets would be in excess of book value if the related environmental legacy costs and collective agreements could not be separated from the assets.

63 Before turning to that exercise, I would also observe that test (c) is also disjunctive. There is an insolvency condition if the total obligation of the debtor exceed either (i) a fair valuation of its assets or (ii) the proceeds of a sale fairly conducted under legal process of its assets.

64 As discussed above and confirmed by Stephen, if there were a sale under legal process, then it would be unlikely, especially in this circumstance that values would be enhanced; in all probability they would be depressed from book value. Stephen took the balance sheet GAAP calculated figure of equity at November 30, 2003 as $804.2 million. From that, he deducted the loss for December 2003 - January 2004 of $17 million to arrive at an equity position of $787.2 million as at the date of filing.

65 From that, he deducted, reasonably in my view, those "booked" assets that would have no value in a test (c) sale namely: (a) $294 million of future income tax recourse which would need taxable income in the future to realize; (b) $57 million for a write-off of the Platemill which is presently hot idled (while Locker observed that it would not be prohibitive in cost to restart production, I note that neither Stephen nor Vaughn were cross examined as to the decision not to do so); and (c) the captialized deferred debt issue expense of $3.2 million which is being written off over time and therefore, truly is a "nothing". This totals $354.2 million so that the excess of value over liabilities before reflecting obligations not included in the financials directly, but which are, substantiated as to category in the notes would be $433 million.

66 On a windup basis, there would be a pension deficiency of $1252 million; however, Stephen conservatively in my view looked at the Mercer actuary calculations on the basis of a going concern finding deficiency of $656 million. If the $1252 million windup figure had been taken, then the picture would have been even bleaker than it is as Stephen has calculated it for test (c) purposes. In addition, there are deferred pension costs of $198.7 million which under GAAP accounting calculations is allowed so as to defer recognition of past bad investment experience, but this has no realizable value. Then there is the question of Employee Future Benefits. These have been calculated as at December 31, 2003 by the Mercer actuary as $909.3 million but only $684 million has been accrued and booked on the financial statements so that there has to be an increased provision of $225.3 million. These off balance sheet adjustments total $1080 million.

67 Taking that last adjustment into account would result in a *negative* equity of ($433 million minus $1080 million) or *negative* $647 million. On that basis without taking into account possible reductions in capital assets as dealt with in the somewhat flawed Exhibit E nor environmental and other costs discussed above, Stelco is insolvent according to the test (c). With respect to Exhibit E, I have not relied on it in any way, but it is entirely likely that a properly calculated Exhibit E would provide comparators (also being sold in the U.S. under legal process in a fairly conducted process) which tend to require a further downward adjustment. Based on test (c), Stelco is significantly, not marginally, under water.

68 In reaching my conclusion as to the negative equity (and I find that Stephen approached that exercise fairly and constructively), please note my comments above regarding the possible assumption of pension obligations by the purchaser being offset by a reduction of the purchase price. The 35% adjustment advocated as to pension and employee benefits in this regard is speculation by the Union. Secondly, the Union emphasized cash flow as being important in evaluation, but it must be remembered that Stelco has been negative cash flow for some time which would make that analysis unreliable and to the detriment of the Union's position. The Union treated the $773 million estimated contribution to the shortfall in the pension deficiency by the Pension Benefits Guarantee Fund as eliminating that as a Stelco obligation. That is not the case however as that Fund would be subrogated to the claims of the employees in that respect with a result that Stelco would remain liable for that $773 million. Lastly, the Union indicated that there should be a $155 million adjustment as to the negative equity in Sub Applicants when calculating Stelco's equity. While Stephen at Q. 181-2 acknowledged that there was no adjustment for

that, I agree with him that there ought not to be since Stelco was being examined (and the calculations were based) on an unconsolidated basis, not on a consolidated basis.

69 In the end result, I have concluded on the balance of probabilities that Stelco is insolvent and therefore it is a "debtor company" as at the date of filing and entitled to apply for the CCAA initial order. My conclusion is that (i) BIA test (c) strongly shows Stelco is insolvent; (ii) BIA test (a) demonstrates, to a less certain but sufficient basis, an insolvency and (iii) the "new" CCAA test again strongly supports the conclusion of insolvency. I am further of the opinion that I properly exercised my discretion in granting Stelco and the Sub Applicants the initial order on January 29, 2004 and I would confirm that as of the present date with effect on the date of filing. The Union's motion is therefore dismissed.

70 I appreciate that all the employees (union and non-union alike) and the Union and the International have a justifiable pride in their work and their workplace - and a human concern about what the future holds for them. The pensioners are in the same position. Their respective positions can only be improved by engaging in discussion, an exchange of views and information reasonably advanced and conscientiously listened to and digested, leading to mutual problem solving, ideas and negotiations. Negative attitudes can only lead to the detriment to all stakeholders. Unfortunately there has been some finger pointing on various sides; that should be put behind everyone so that participants in this process can concentrate on the future and not inappropriately dwell on the past. I understand that there have been some discussions and interchange over the past two weeks since the hearing and that is a positive start.

Motion dismissed.

APPENDIX

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

ORIONIS CORPORATION Applicant and **ONTARIO GRAPHITE, LTD.** Respondent

Court File No: CV-20-00634195-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST
PROCEEDING COMMENCED AT: TORONTO

BOOK OF AUTHORITIES OF THE APPLICANT
(Comeback Hearing; Returnable Feb. 20, 2020)

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