

**IN THE SUPREME COURT OF NOVA SCOTIA**  
**Citation: Federal Gypsum Company (Re), 2007 NSSC 347**

**Date:** 2007/11/05

**Docket:** S. H. No. 285667

**Registry:** Halifax

**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 the  
Applicant, Federal Gypsum Company

**Judge:**                    The Honourable Justice A. David MacAdam

**Heard:**                    November 5, 2007, Orally, in Halifax, Nova Scotia

**Written  
Decision:**                January 29, 2008

**Counsel:**                Maurice P. Chaisson/Graham Lindfield,  
                                for the Federal Gypsum Company  
                                Carl Holm, Q.C. for BDO Dunwoody Goodman Rosen Inc.  
                                Thomas Boyne, Q.C. for the Royal Bank of Canada  
                                Robert Sampson/Robert Risk for Enterprise Cape Breton  
                                Corporation and Cape Breton Growth Fund Corporation  
                                Michael Pugsley for Her Majesty in Right of the Province of  
                                Nova Scotia (Nova Scotia Economic Development) and Nova  
                                Scotia Business Incorporated  
                                Michael Ryan, Q.C. for Black & McDonald Limited

**By the Court:**

[1] Federal Gypsum Company, (herein “the Company” or “the Applicant”), having been granted a stay of proceedings pursuant to S. 11 of the *Companies Creditors Arrangement Act*, R.S.C. 1985, c. C-25 (herein “*CCAA*”), and, subsequently approval of arrangements for debtor in possession (herein “DIP”) financing and an Order providing for extension of the Stay Termination Date set out in the initial Order, now applies for approval of arrangements for additional DIP financing.

[2] The initial Stay Order provided for a 30-day Stay of Proceedings pursuant to s. 11(3) of the *CCAA*. The initial DIP financing application authorized DIP financing in the principal sum of \$350,000.00. The time for filing the Plan of Arrangement under the *CCAA* and the Stay Termination Date were extended to November 29, 2007 at 4:00 p.m, by Order dated October 23, 2007. The Order also provided that “the Company shall file an Application before this Honourable Court relating to the consideration of further debtor in possession financing for a hearing on November 5, 2007 at 9:30 a.m.” The Order also stipulated that the extension of the Stay Termination Date to November 29, 2007 was “subject to the

right of the creditors of the Company to request a review and reconsideration” of the October 23 Order on the application for further DIP financing.

[3] The Company now seeks an increase in the DIP financing from the original authorized \$350,000.00 to \$1,500,000.00.

[4] Appearing on the Company’s application were a number of secured creditors, including the Royal Bank of Canada, (herein “Royal Bank”), Cape Breton Growth Corporation, (herein “CBGC”), and Enterprise Cape Breton Corporation, (herein “ECBC”), (herein collectively referred to as the “Federal Crown Corporations”); Nova Scotia Business Inc. (herein “NSBI”) and Nova Scotia - Office of Economic Development (herein “NSOED”) (herein collectively referred to as the “Nova Scotia Crown Corporations”), each of whom hold, or purport to hold, first secured charges on some of the assets of the Company, as do the Federal Crown Corporations; and Black & McDonald Limited, (herein “BML”) who purport to hold a subordinate secured charge on assets of the Company.

The CCAA

[5] The relevant provisions of Section 11 of the CCAA are as follows:

11. (1) **Powers of court** - Notwithstanding anything in the *Bankruptcy and Insolvency Act* or the *Winding-up Act*, where an application is made under this Act in respect of a company, the court, on the application of any person interested in the matter, may, subject to this Act, on notice to any other person or without notice as it may see fit, make an order under this section.
  
- (2) **Initial Application** - An application made for the first time under this section in respect of a company, in this section referred to as an 'initial application' shall be accompanied by a statement indicating the projected cash flow of the company and copies of all financial statements, audited or unaudited, prepared during the year prior to the application, or where no such statements were prepared in the prior year, a copy of the most recent such statement.
  
- (3) **Initial application court orders** - A court may, on an initial application in respect of a company, make an order on such terms as it may impose, effective for such period as the court deems necessary not exceeding thirty days,
  - (a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);
  
  - (b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

(4) **Other than initial application court orders** - A court may, on an application in respect of a company other than an initial application, make an order on such terms as it may impose,

(a) staying, until otherwise ordered by the court, for such period as the court deems necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

(5) **Notice of orders** - Except as otherwise ordered by the court, the monitor appointed under section 11.7 shall send a copy of any order made under subsection (3), within ten days after the order is made, to every known creditor who has a claim against the company of more than two hundred and fifty dollars.

(6) **Burden of proof on application** - The court shall not make an order under subsection (3) or (4) unless

(a) the applicant satisfies the court that circumstances exist that make such an order appropriate; and

(b) in the case of an order under subsection (4), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

## The Law

[6] The purpose of the CCAA was commented on by Justice Turnbull of the New Brunswick Court of Appeal in *Juniper Lumber Co., Re*, [2000] N.B.J. No. 144, at para. 1:

The principal purpose of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the 'CCAA'), 'is to facilitate the making of a compromise or arrangement between an insolvent debtor company and its creditors to the end that the company is able to continue in business ... When a company has recourse to the C.C.A.A. the court is called upon to play a kind of supervisory role to preserve the status quo and to move the process along to the point where a compromise or arrangement is approved or it is evident that the attempt is doomed to failure.' See *Arrangements Under the Companies' Creditors Arrangement Act* by Goldman, Baird and Weinszok (1991), 1 C.B.R. (3d) 135 at p. 201 where the authors cite Thackray, J. approvingly quoting Gibbs, J.A. from the cases cited on that page. In New Brunswick, the Court of Queen's Bench is defined by the CCAA as the Court to play the 'kind of supervisory role.' The CCAA has a remedial purpose and, therefore, must be interpreted in a broad and liberal fashion. See pages 137-138 in the article previously cited. More often than not time is critical. And, in order to maintain a status quo while attempts are made to determine if a successful compromise or arrangement can be reached, the courts are granted certain powers in s. 11 to hold creditors at bay.

[7] Justice Glennie of the New Brunswick Court of Queen's Bench in *Simpson's Island Salmon Ltd., Re*, 2006 NBQB 279, at para. 20, after referencing

*Juniper Lumber Co., referred to Lehndorff General Partner Ltd., Re*, [1993] O.J.

No. 14 (Ont. C.J. - Gen. Div.), at paras. 5 and 6, where Farley, J. said:

The CCAA is intended to facilitate compromises and arrangements between companies and their creditors as an alternative to bankruptcy and, as such, is remedial legislation entitled to a liberal interpretation. It seems to me that the purpose of the statute is to enable insolvent companies to carry on business in the ordinary course or otherwise deal with their assets so as to enable a plan of compromise or arrangement to be prepared, filed and considered by their creditors and the court. In the interim, a judge has a great discretion under the CCAA to make order so as to effectively maintain the status quo in respect of an insolvent company while it attempts to gain the approval of its creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors. ...

The CCAA is intended to provide a structured environment for the negotiation of compromises between a debtor company and its creditors for the benefit of both. Where a debtor company realistically plans to continue operating or to otherwise deal with its assets but it requires the protection of the court in order to do so and it is otherwise too early for the court to determine whether the debtor company will succeed, relief should be granted under the CCAA. ...

## **Background**

### *(A) The Initial Application*

[8] On the initial application, the Court having been satisfied the company met the requirements for the filing under the *CCAA*, in that it was, on the evidence tendered, “insolvent” and had total claims exceeding \$5,000,000.00, and being

further satisfied that the burden stipulated in s. 11(6) had been met, an Order providing for a Stay of Proceedings was issued.

*(B) The Initial DIP Financing*

[9] Shortly after the Stay Order was issued, the Company filed the application for the initial DIP financing in the sum of \$350,000.00. Counsel for the company acknowledged the omission in the CCAA of any specific authorization sanctioning DIP financing and granting “super-priority” over existing secured, as well as unsecured, debt. Counsel referenced the legal principles cited by Justice C. Campbell in *Manderley Corp., Re* (2005) 10 C.B.R. (5<sup>th</sup>) 48, at para 18 where he observes:

The operative legal principles are set out in the following quotations from Houlden & Morawetz' *Bankruptcy & Insolvency Analysis* (Carswell, 2004), section N16 - - Stay of Proceedings[sic] - - CCAA - - at page 18:

Although the C.C.A.A. makes no provision for DIP financing, it seems to be well established that, under its inherent powers, the court may give a priority for such financing and for professional fees incurred in connection with the working out of a C.C.A.A. plan.



For the court to authorize DIP financing, there must be cogent evidence that the benefit of the financing clearly outweighs the prejudice to the lenders whose security is being subordinated to the financing: ...

The court can create a priority for the fees and expenses of a court-appointed monitor ranking ahead of secured creditors so long as they are reasonably incurred in connection with the restructuring of the debtor corporation and there is a reasonable prospect of a successful restructuring: ...

[10] At para 19 Justice Campbell continues:

In *Skydome Corp., Re*, 1998 CarswellOnt 5922, 16 C.B.R. (4<sup>th</sup>) 118 (Ont. Gen. Div. [Commercial List] ), Blair J. (as he then was) dealt with the issue of 'super-priority' financing in the context of the specific use to be made of the funds where he was satisfied that the priority accorded the DIP financing would not prejudice the secured creditors. At paragraph 13 he said:

I am satisfied that the Court has the authority either under s. 8 of the CCAA or under its broad discretionary powers in such proceedings, to make such an order. This is not a situation where someone is being compelled to advance further credit. What is happening is that the creditor's security is being weakened to the extent of its reduction in value. It is not the first time in restructuring proceedings where secured creditors - - in the exercise of balancing the prejudices between the parties which is inherent in these situations - - have been asked to make such a sacrifice. Cases such as *Re Westar Mining Ltd.* (1992), 14 C.B.R. (3d) 88 (B.C. S.C.) are examples of the flexibility which courts bring to situations such as this. ...

[11] To similar effect Wachowich J. in *Hunters Trailer & Marine Ltd., Re* (2001), 295 A.R. 113 (Q.B.), noted, at para. 32, the necessity to balance the benefit

of such financing with the potential prejudice to the existing secured creditors.

Justice Glennie in *Re Simpson's Island Salmon Ltd., supra*, at paras. 16 - 19 held:

In order for DIP financing with super-priority status to be authorized pursuant to CCAA, there must be cogent evidence that the benefit of such financing clearly outweighs the potential prejudice to secured creditors whose security is being eroded. See *United Used Auto & Truck Parts Ltd., Re*, [1999] B.C.J. No. 2754 (B.C.S.C. [ In Chambers] ), affirmed [2000] B.C.J. No. 409 (B.C. C.A.)

DIP financing ought to be restricted to what is reasonably necessary to meet the debtors urgent needs while a plan of arrangement or compromise is being developed.

I am satisfied on the evidence before me that Simpson's Island and Tidal Run have a viable basis for restructuring. The amount of the DIP facility has been restricted to what is necessary to meet short-term needs until harvest.

A Court should not authorize DIP financing pursuant to the CCAA unless there is a reasonable prospect that the debtor will be able to make an arrangement with its creditors and rehabilitate itself. In this case the Monitor has advised the Court that there is a reasonable prospect that Simpson's Island and Tidal Run will be able to make such arrangements with their creditors.

[12] In his written submission counsel for the company, in reference to the three issues for review outlined by Justice Glennie, commented that “[e]ssentially, the court must engage in the balancing act that is the hallmark of DIP financing, as declared by C. Campbell, J. in *Manderley ...* at para. 27, weighing the benefit and prejudice referred to by Glennie, J.”

[13] The secured creditors, with the exception of the Royal Bank, neither consented nor strenuously objected to the initial DIP financing sought by the Company. The Royal Bank, on the other hand, objected, on the basis that the funding of the ongoing operations of the company could very well be at the expense of its security on the receivables and inventory. Nevertheless, having balanced prejudice to the secured creditors, in this instance particularly to the Royal Bank, and the benefit of providing financing to enable the Company to pursue a Plan of Arrangement, and on being satisfied the sought-for DIP financing and resulting super-priority were reasonably necessary to meet the Company's immediate needs and there was a reasonable prospect the Company would be able to make arrangements with its creditors and thereby rehabilitate itself, this Court allowed the application.

*(C) The First Extension*

[14] At the expiration of the initial Stay Termination date, the Company applied for an extension, which application was generally opposed by the secured creditors. The Application included a further Affidavit by one of the Directors and

Officers of the Company, as well as a further report from the Monitor. In para. 4.7, the Monitor reported:

Having met with Federal and its legal counsel, and having had preliminary discussions with them as to the general principles and format of a Plan of Arrangement, and having considered the progress made in financing and sales opportunities, and having had initial discussions with senior secured creditors, the Monitor concludes that Federal has acted, and continues to act, in good faith and with due diligence and, if given sufficient time by This Honorable (sic) Court, should be able to file a Plan of Arrangement under CCAA that will have a significant chance of being successful.

[15] Included among the Monitor's recommendations was the observation that the Company "... must make an application for an increase in the DIP financing level and such other matters as may relate thereto".

[16] In *Cansugar Inc., Re*, 2004 NBQB7, at paras 8 and 9, Justice Glennie in respect to applications for extension of stay termination dates, after referencing ss. 11(4) and (6) of the CCAA, stated:

In *The 2004 Annotated Bankruptcy & Insolvency Act*, Houlden & Morawetz state at page 1126:

To obtain an extension, the application must establish three pre-conditions:

- (a) the circumstances exist that make the order appropriate;
- (b) that the applicant has acted and continues to act in good faith; and
- (c) that the applicant has acted and continues to act with due diligence.

In my opinion, the requirements of section 11(6) of the C.C.A.A. have been satisfied in this case. The continuation of the stay is supported by the overriding purpose of the C.C.A.A., which is to allow an insolvent company a reasonable period of time to reorganize and propose a plan of arrangement to its creditors and the Court, and to prevent maneuvers for positioning among creditors in the interim.

[17] In support of the application for the extension, counsel referenced para. 17 of the Affidavit of Mr. Simpson, where he states that:

An extension of the Stay of Termination Date would allow the Company to accomplish the following:

- (a) continue with its recent efforts to improve sales, which are expected to yield positive results;
- (b) provide for additional debtor-in-possession financing to service the Company's cash flow needs in the short and medium term until the Plan is presented to the Company's stakeholders;
- (c) complete the appraisal of the assets of the Company;

- (d) complete cash flow forecasts and income statement and balance sheet projections for the 2008, 2009 and 2010 years; and
- (e) finalize the elements of the Plan.

[18] At para 18 Mr. Simpson continues:

I believe that if the Stay Termination Date is not extended, some of the creditors of the Company will commence proceedings against the Company in relation to the enforcement of their security. Such proceedings would be highly prejudicial to the interests of the Company and would significantly impair the Company's ability to complete a successful restructuring.

[19] Mr. Simpson's Affidavit, in outlining the present circumstances and the efforts of the company since the date of the initial order, also states that the Company "... is presently formulating a plan to present to its various stakeholders - including its creditors". Counsel notes the Company is arranging for an appraisal of its assets and negotiating with a lender to provide additional financing during the "near and medium term". Counsel suggests these factors demonstrate that:

... the Company has been proceeding diligently and in good faith since the Initial Order to assemble the elements of a plan to be presented to its stakeholders. There will be several elements to this plan and the Company requires additional

time to bring these elements together. The Company's majority shareholder is motivated by the single goal of putting together a plan which will ensure the survival of the Company and, in so doing, protect, to the fullest extent possible, the interests of the stakeholders as a whole.

[20] Counsel references *San Francisco Gifts Ltd., Re*, 2005 ABQB 91, where, at para. 28, Topolniski. J. comments on the supervisory role of the Court on such an application:

The court's role during the stay period has been described as a supervisory one, meant to: '*... preserve the status quo and to move the process along to the point where an arrangement or compromise is approved or it is evident that the attempt is doomed to failure.*' That is not to say that the supervising judge is limited to a myopic view of balance sheets, scheduling of creditors' meetings and the like. On the contrary, this role requires attention to changing circumstances and vigilance in ensuring that a delicate balance of interests is maintained.

[21] The application for an extension of the Stay Termination Date was opposed on the basis that the performance by the Company did not generate confidence it had turned the corner and was likely to survive. The objecting creditors viewed the performance of the Company as further prejudicing their position in respect to the secured positions they held on the various assets of the company. They took this view, notwithstanding the Monitor's assessment that the Company, by its actions, appeared to be acting in good faith and with due diligence and moving forward towards the preparation of a Plan of Arrangement, and that the actual net

cashflow of the Company was not adverse to the cashflow plan as presented on the initial Order. On the Application for the Stay Extension, counsel for the Nova Scotia Crown Corporations did not object to the extended Stay, but expressed a concern about the proposed increase in the DIP financing.

[22] Considering the position of the creditors and the representations on behalf of the Company, the Stay Termination Date was extended to November 29, 2007 with the proviso that on the Application for further DIP financing the creditors could request a review and reconsideration of the extension.

### **Issue**

[23] At issue is whether the Company's application for approval of Arrangements for additional DIP financing should be approved, including the proposed payout of the Royal Bank operating loan, and whether the Court should reconsider the extension of the Stay Termination Date to November 29, 2007.

### **The Present Applications**



### **Reconsidering the Extension of the Stay Termination Date**

[24] In respect to the Company's application to extend the Stay Termination Date, counsel on behalf of the Royal Bank had indicated the Bank's opposition both in writing and in oral submission. Counsel noted the burden of proof was on the Applicant. Counsel for the Company suggested circumstances existed that made it appropriate to extend the initial Order, in that the Applicant had acted, and continued to act in good faith and with due diligence. In this respect counsel refers to *Re Inducon Development Corp.* (1992), 8 C.B.R. (3d) 306, (Ont. C.J. - Gen. Div.), where Farley, J. observed :

The good faith and due diligence of the Applicant are not questioned.

[25] On the reconsideration application, counsel for the Royal Bank acknowledged that neither the good faith nor due diligence of the Applicant were questioned, but said the Company had failed to show circumstances that made it appropriate to extend the initial Order. Counsel suggested that to cover the losses for the first seven months of 2007 the Company would have to increase its net sales by over 65%, and if one were to include all expenses and only the repayment

of \$1,000,000.00 per year on the total liabilities of more than \$32,000,000.00, the Applicant would have to increase its net sales by 92%. Counsel noted the difficulties the Company has had in marketing its products and that in fact there has been a “decrease in sales from expected levels with a resulting decrease in accounts receivables”. Counsel added that in the Monitor’s second report he indicated sales were over \$150,000.00 less than budget and expressed concern about the trend in sales. Counsel submitted that there is no evidence of a plan, referring again to reasons of Justice Farley in *Inducon Development Corp, supra*, where he stated:

[W]hile it is desirable to have a formalized plan when applying, it must be recognized as a practical matter that there may be many instances where only an outline is possible. I think it inappropriate, absent most unusual and rare circumstances, not to have a plan outline at a minimum, in which case then I would think that there would be a requisite for the germ of a plan.

[26] Counsel for the Royal Bank suggested it is inappropriate to continue CCAA protection where the Company does not have, “at the least, a minimum outline of a plan”.

[27] In response to the Company's suggestion that the creditors "will not be materially prejudiced as the company continues to operate ....", Counsel said there is real prejudice, including:

- (a) interference with the rights of secured creditors to deal with their security and to maximize their recovery;
- (b) changing market conditions and the loss of potential purchasers of the assets;
- (c) deterioration in the value of assets through on-going use;
- (d) in the case of Royal Bank of Canada, the eroding of and loss of its security interest through the collection and use of accounts receivable [sic] to fund the operations of the Applicant during the Stay;
- (e) costs of professionals in maintaining these proceedings, which in the case of the Applicant are recognized to be as great as \$300,000;
- (f) professionals costs to the creditors; and
- (g) delay with regard to unsecured creditors in recognizing losses and the decisions that they must make in dealing with their own creditors on a go forward basis.

[28] Counsel notes as unique the reality that the Company has never been profitable, whereas in many of the cases where *CCAA* orders are granted, the

Companies have been in business for some period of time and, through circumstances, have suffered adversity which may be overcome through forgiveness and restructuring of debt obligations and the injection of equity to enable them to return to a state of profitability. The Company, counsel suggests, has never generated enough sales to even meet its operating expenses. Counsel adds that no evidence has been presented to the Court to indicate such a level of sales can be reached. As a result, counsel concludes, the Company has no reasonable expectation of reaching the required level of sales.

[29] Notwithstanding the forceful submission of counsel for the Royal Bank, it is clear that although net sales have declined, the Company has also incurred lower expenses and has used less of the authorized DIP financing than had been projected in the cashflow projections filed on the initial DIP financing application. Like with the Monitor, I am concerned with the failure of the Company to meet the projected sales. There are, however, some positive indications from the information filed in the Monitor's report and outlined in the Affidavit of Rhyne Simpson, Jr., President and a Director of the Applicant. I am not satisfied the Company has reached the stage of "the last gasp of a dying company" or is in its "death throes", although clearly any Plan of Arrangement will require

compromise and cooperation between the Company and its stakeholders. During the course of submissions, counsel for the Company acknowledged that if additional DIP financing was not obtained the inevitable consequence would be the demise of the Company. The effect on the Company of terminating the extension of the Termination Date, as it relates to the opportunity for the preparation and presentation of a Plan of Arrangement, is evident. The prejudice to the creditors, although evident, is perhaps not so fatal. Although not necessarily indicative of the position of the Royal Bank, should, in due course, the Company fail, nevertheless on the financial information filed by the Monitor from information obtained from the Company's officers, it would not appear that there has been a substantial deterioration in the Royal Bank's secured position to date.

[30] As a consequence I am prepared to grant the Order continuing the Stay Termination Date until November 29<sup>th</sup>, 2007, provided the Company is successful on the application for additional DIP financing.

### **The Additional DIP Financing**

[31] On the Application to extend the Stay Termination Date and to set the date for filing the Plan of Arrangement, counsel for the Company acknowledged that if the Company was unsuccessful in obtaining approval of arrangements for additional DIP financing, notwithstanding the extension, the Company would not be able to continue in operation while preparing and presenting to its creditors its proposed Plan of Arrangement. On the Application for the \$1,500,000.00 DIP financing, the Monitor appointed on the initial application, in his third report to the Court, indicated the purpose was to replace the previous DIP lender, pay out the Royal Bank working capital loan, and provide additional DIP funds to allow the Company to continue operations and provide time to finalize and file a Plan of Arrangement for consideration by the creditors. The Monitor reported that its weekly cashflow projections, as prepared by the Company, indicated the requirement for DIP financing for the week of November 26, 2007 would be approximately \$83,000.00 in excess of the present DIP financing approval limit. The report further indicated that beyond the Stay Termination Date of November 29, 2007 the requirement for DIP financing would increase significantly in the month of December 2007.

[32] With the sole exception of the Royal Bank, the secured creditors oppose the application for additional DIP financing. The Royal Bank, in view of the stipulated intention to use the additional DIP financing to pay down its working capital loan, leaving only a second loan secured on certain leases, does not oppose the additional DIP financing. Absent the provision for repayment of its working capital loan, it is clear from the representations of counsel, both on this and earlier applications, that the Royal Bank would not consent to nor support the request for additional DIP financing.

[33] On the application, counsel for the Company advised that the proposed DIP lender had stipulated certain changes in the terms of the proposed financing to require the first DIP lender to advance the remainder of the amounts authorized under the initial DIP Order and that the full amount of \$350,000.00 be subordinated to its charge. There were changes relating to the "borrowing base" for the loans and a requirement that the priority of the "Administration Charge", which priority was provided for in the initial Order, was not to exceed the sum of \$75,000.00. During the course of the application counsel also advised that other changes had been approved by the DIP lender, including verification of the

amount upon which the lender was entitled to charge fees over and above the interest provided for in the offer of financing.

[34] Counsel for the applicant, referencing the comment by C. Campbell, J. in *Re Manderley Corp., supra*, at para 27, acknowledged the Court must engage in “the balancing act that is the hallmark of DIP financing”. He notes Justice Glennie applied this balancing in considering the approval of super-priority funds, beyond those initially requested, when, in *Simpson’s Island Salmon Ltd. Re*, 2006 NBQB 244, at para 9, he declared:

As stated by MacKenzie J.A. in *United Used Auto & Truck Parts Ltd., Re* (2000), 16 C.B.R. (4<sup>th</sup>) 141 (B.C. C.A.):

[12] ... the CCAA’s effectiveness in achieving its objectives is dependent on a broad and flexible exercise of jurisdiction to facilitate a restructuring and continue the debtor as a going concern in the interim.

[28] The object of the CCAA is more than the preservation and realization of assets for the benefits of creditors, as several courts have underlined. In *Chef Ready Foods*, Giggs J.A. said that the primary purpose is to facilitate an arrangement to permit the debtor company to continue in business and to hold off creditors long enough for a restructuring plan to be prepared and submitted for approval. The court has a supervisory role and the monitor is appointed ‘to monitor the business and financial affairs of the company’ for the court.



[35] Justice Glennie was concerned with an application for an increase in the “Administrative Charge”, for which priority was granted, to the advisors retained to formulate and present the restructuring plan. He determined that failure to grant the increase would result in the applicants no longer being able to continue their attempts at restructuring. He referred to the decision of Justice Wachowich, also in respect to an administrative charge, in *Hunters Trailer & Marine Ltd., supra*, denying an increase in the amount of DIP financing. He found the applicant had not met the onus under s. 11(6) (a) of the *CCAA* to establish that a stay would be appropriate in the circumstances. At para 10 he observed:

In my view, the evidence provided by Hunters does not show that the benefits of DIP financing will clearly outweigh potential prejudice to the Objecting Creditors. While DIP financing is the only means for Hunters to continue operating, it is impossible to conclude that this short-term benefit will culminate in Hunters’ financial recovery, due to a number of deficiencies in the evidence.

[36] Justice Wachowich continued by identifying particular deficiencies such as the absence of appraisals, the absence of current financial information on the Company, the absence of verification of the Company’s cashflow projections by the Monitor and uncertainty as to the value of one of the major assets. Counsel suggests that in the present instance these deficiencies do not exist, in that an appraisal has been obtained, the current financial information is available on an

ongoing basis, and the Monitor is being provided with continuing opportunities to verify the Company's cashflow projections and has done so. Counsel also suggests the other deficiency noted by Justice Wachowich, the uncertainty as to the value of a major asset, is not an issue in the current circumstance.

[37] Counsel for the Company, suggesting that DIP financing "is merely prolonging the inevitable", cites para. 13 of *Hunters Trailer & Marine Ltd.*, 2000 ABQB 952:

Another consideration in assessing the benefit of DIP financing is that even if Hunters' projected cashflows are accurate, they show a continuing net deficit, suggesting that the benefit of DIP financing is merely prolonging the inevitable. Even as of September 2001, following the months when the volume of Recreational Vehicle ('RV') sales is highest, Hunters expects a cash flow deficit. After September, the RV sales will slow down significantly as Hunters enters the low season, so cash flow is not likely to increase after September. Hunters can expect continuing difficulties in meeting operating expenses well into the foreseeable future. The sources of Hunters' cash flow problems, as identified by Blair Bondar, the company president, will likely continue to exist. Mr. Bondar states that RV sales have decreased as a result of, in part, increasing gas prices, a weak Canadian dollar, and increased competition. Hunters has no control over these systemic problems, and there is no evidence or reason to believe that they will be resolved in the foreseeable future. As a result, I am not convinced that the cash flow projections themselves are accurate. The Monitor does not verify the accuracy or reasonableness of the projections. Therefore, it is impossible to conclude that the DIP financing will benefit Hunters and its creditors in the long run.

[38] Counsel says the current circumstance can be distinguished for a number of reasons, including that the projected cashflow statements “do not disclose uninterrupted deficits, and those deficits that exist for the most part are minimal.”

Counsel’s submission continues:

... The sources of the Company’s cash flow problems are not expected to continue to exist, or at least to have as severe an effect as they did during the month of October, as noted at paragraph 25 of the Additional DIP Affidavit. Finally, as noted above, the Monitor has verified the reasonableness of the Company’s cash flow projections. All of the above circumstances suggest, contrary to those facing Wachowich J. in *Hunters (2000)* (*supra*), that additional DIP financing will benefit the Company and its creditors in the long run, as those funds will allow the Company to take advantage of the opportunities presented, and thereby ultimately bolster its efforts to finalize and present a viable restructuring plan. It is submitted that none of the myriad reasons by Wachowich J. for denying further DIP financing are present in the current situation.

[39] Counsel suggests the additional DIP financing is a necessary cost of ensuring there can be a meaningful discussion between the stakeholders about the restructuring plan. Counsel recognizes that any protection afforded by the CCAA, with its attended super-priority, will necessarily have a prejudicial effect on the Company’s creditors. As counsel suggests, what must be examined is whether such prejudice is more than outweighed by the prejudice to the Company and its stakeholders should the requested DIP financing be denied, given that, as counsel suggests, “it would most likely have to cease operations in that instance.” Counsel

suggests the Affidavit filed in support of the Application “provides clear evidence of improving prospects for the Company, as well as considerable effort on its part to build a sustainable business, the ultimate goal of the CCAA restructuring process”. Having considered the Monitor’s reports and filed documents, including affidavits, together with the representations of Counsel, I am satisfied it is appropriate to continue CCAA protection to enable the Company to finalize preparation of the Plan and its presentation to the creditors. In view of the need for additional DIP financing to enable the Company to continue in operation, while the Plan is considered and voted upon by the creditors, the Company is granted approval for additional DIP financing.

### **Payout of the Royal Bank**

[40] Counsel for the Company’s submission recognized the possibility that some of the secured creditors would object to the application and, in particular, to the proposed buy-out of the Royal Bank’s operating line of credit. Counsel referenced the comments of Farley, J. in *Re Dylex Limited* (1995), 31 C.B.R. (3d) 106, to the effect that the mere fact a significant secured creditor objects to such financing should in no way preclude the Court’s ability to approve DIP financing. Counsel

then references *Hunters Trailer Marine Ltd., Re*, (2000), 295 A.R. 113, at para 32, where the Court stated that “if super-priority cannot be granted without the consent of secured creditors, the protection of the CCAA effectively would be denied a debtor company in many cases.”

[41] Counsel’s submission continues:

... the specific issue of the Court’s ability to approve an agreement between a CCAA debtor and one or more, though less than all, of its creditors was recently reviewed by the Alberta Court of Appeal in *Re. Calpine Canada Energy Ltd.* 2007 ABCA 266. As C. O’Brien J.A. noted,

*The power to approve such transactions during the stay is not spelled out in the CCAA. As has often been observed, the statute is skeletal. The approval power in such instances is usually said to be found either in the broad powers under section 11(4) to make orders other than on an initial application to effectuate the stay, or in the court’s inherent jurisdiction to fill in gaps in legislation so as to give effect to the objects of the CCAA, including the survival program of the debtor until it can present a plan: Re Dylex Ltd., (1995), 31 C.B.R. (3d) 106 at para 8 (Ont. Gen. Div.)*

In the result the Court of Appeal upheld the ruling of B.E. Romaine J. at the Court of Queen’s Bench: 2007 ABQB 504. As Justice Romaine set out,

*... Settling with one or two claimants will invariably have an effect on the size of the estate available for other claimants. The test of whether such an adjustment results in fair and reasonable requires the Court to look to the benefits of the settlement to the creditors as a whole, to consider the prejudice, if any, to the objecting creditors specifically and to ensure that*

*rights are not unilaterally terminated or unjustly confiscated without the agreement or approval of the affected creditor.*

...

*... It is clear from the case law that Court approval of settlements and major transactions can and often is given over the objections of one or more parties. The Court's ability to do this is a recognition of its authority to act in the greater good consistent with the purpose and spirit and with the confines of the legislation.*

[42] In his Affidavit filed on this application, Mr. Simpson, at para. 16, deposes:

The Company is pursuing this repayment so as to afford the best chance of success for its restructuring plan (the 'Plan') when it is presented to creditors, and thereby the best chance of a reasonable resolution. Throughout the Company's proceedings under the CCAA to this point, the Royal Bank has been consistently vocal in its opposition to the restructuring process. It is most likely that the Royal Bank's continued participation in the process will only hinder it, necessitating the use of further time and the expenditure of additional costs in order to ultimately achieve a fair restructuring, a result that will be most beneficial to the Company, and given the limited alternatives, most beneficial to the creditors as a whole. It is for these reasons that the Company considers repayment of the operating facility to be in the best interests of all stakeholders.


[43] After referencing para 16 of Mr. Simpson's Affidavit, Counsel suggests that in view of the Royal Bank's opposition to the process, and in view of the serious discussions and negotiations that will occur between the Company and its creditors:

... For the attainable and beneficial goal of a successful restructuring to be achieved, it is the Company's position that the Royal Bank should likely be removed from active participation through the retirement of its operating line, and that this Court is empowered to do so either under s. 11(4) of the CCAA or by way of its inherent jurisdiction.

[44] On being examined, Mr. Simpson indicated, in response to the question why provide for the payout of the Royal Bank operating line, that it would "make life easier, but is not necessary". To similar effect, counsel for the Company in his oral submission acknowledged that the rejection of the proposal to pay out the Royal Bank operating line would not appear to be fatal to the proposed restructuring. In the circumstances, it is clear that the success of the restructuring and the Plan is not dependent on permitting the repayment of this single creditor. As such, there is really no justification for favouring the Royal Bank by authorizing the repayment of its operating line from the DIP financing. The request to pay out the Royal Bank operating line is therefore denied.

**Conclusion**

[45] The extension of the Stay to November 29, 2007 is confirmed and the Company is authorized to draw down DIP financing in the sum of \$475,00.00. The request to pay out the Royal Bank from the DIP financing is denied.

A handwritten signature in black ink, appearing to read "J. David ...", enclosed within a large, hand-drawn oval.

J.