Court No.: CV-21-00661436-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

2655396 ONTARIO INC.

Applicant

IN THE MATTER OF SECTION 182 OF *THE BUSINESS CORPORATIONS ACT*, R.S.O. 1990, c. B.16, AS AMENDED, AND IN THE MATTER OF A PROPOSED ARRANGEMENT OF 2655396 ONTARIO INC. AND INVOLVING 1776690 ONTARIO INC. COB COUNTRY WAY HEALTH FOOD STORE

FACTUM OF THE PROPOSAL TRUSTEE

Date: 24 January 2022

GOWLING WLG (CANADA) LLP
Barristers and Solicitors
100 King Street West, Suite 1600
Toronto, ON M5X 1G5

E. Patrick Shea (LSO No.: 39655K)
Tel: (416) 369-7399 / Fax: (416) 862-7661
Email: patrick.shea@gowlingwlg.com

Lawyers for the Proposal Trustee

TO: THE SERVICE LIST

FACTUM OF THE PROPOSAL TRUSTEE

PART I – THE MOTION

1. There are two matters before the Court:

   (a) An Application by 2655396 Ontario Inc. ("**2655 Ontario**") seeking an Interim Order pursuant to s. 182(5) of the *Business Corporations Act*, RSO 1990, c. B.16 (the "**OBCA**") in connection with an arrangement (the OBCA Arrangement") involving 1776690 Ontario Inc. cob Country Way Health Food Store ("**Country Way**" or the "**Debtor**") that is included as part of a proposal (the "**Proposal/Arrangement**") filed by Country Way pursuant to Part III of the *Bankruptcy and Insolvency Act*, RSC 1985, c. B-3 (the "**BIA**"); and

   (b) A Motion by Tammy Watts and Brenda Frey ("**Watts/Frey**") seeking: (a) an Order adding them as Respondents on the Arrangement Proceeding and transferring the Arrangement Proceeding to the Superior Court in Sault Ste. Marie so that it can be heard together with an Application commenced by Watts/Frey relating to the sale by them of the shares of Country Way (the "**Watts/Frey Application**"); or, in the alternative, (b) an Order adjourning 2655 Ontario's request for an Interim Order to a later date to permit them to file responding materials.

2. The Interim Order addresses only: (a) voting on the Arrangement by the shareholders of Country Way; and (b) "marrying-up" voting on the Arrangement with voting on the Proposal to reflect the "standard" practice where corporate arrangements are including in proposals under the BIA or plans under the *Companies' Creditors Arrangement Act*, RSC 1985, c. C-36. The Interim Order does not address the final approval of the proposed Arrangement as contemplated by s. 182(5)(f) of the OBCA.

3. This Application was issued on 30 April 2021. The Proposal/Arrangement was filed on 3 May 2021. Watts/Frey filed their Motion in this Application on 3 June 2021. The substantial portion of the Watts/Frey Application was determined on 22 December 2021.

4. MNP Inc. (the "**Trustee**"), in its capacity as trustee named in the Proposal/Arrangement, is not the Applicant on this Application and participates in this matter in its capacity as Trustee.

PART II – THE FACTS

5. Country Way is an Ontario corporation that operates a health food store in Sault Ste. Marie, Ontario from rented premises that are leased from a related company. **[Affidavit of Shonna Saarri sworn 26 April 2021 (the "Saari Affidavit"), para 5]**

6. The Debtor's capital structure is complex. It has four (4) classes of shares: Class A Common (voting) Share, Class A (non-voting) Special Shares, Class B (non-voting) Special Shares and Class C (non-voting) Special Shares. **[Saari Affidavit, para 6]**

7. As at the Summer of 2017, Watts/Frey were the shareholders of Country Way. Pursuant to a Share Purchase Agreement dated 7 August 2017 (the "**SPA**"), Watts/Frey agreed to sell the shares of Country Way to 2595418 Ontario Inc. ("**2595 Ontario**") for $2.2 million. 2595 Ontario paid Watts/Frey $250K on closing and agreed to pay the remaining $1.95 million over 10 years. **[Affidavit of Laurel Saunders[1] sworn 3 June 2021 ("Saunders Affidavit'), para 5 and Exhibit A]**

8. 2595 Ontario borrowed the $250K it paid to Watts/Frey from TNT HoldCo Inc. ("**TNT**"). TNT obtained a guarantee from Country Way and took security over all of Country Way's present and after-acquired property as security. Country Way currently owes TNT $190K. **[Saari Affidavit, para 13]**

9. Watts/Frey did not receive a guarantee from Country Way and took no security over the assets of Country Way to secure the $1.95 million. **[Saari Affidavit, para 12]**

10. 2595 Ontario pledged certain shares of Country Way as security for the payment of the $1.95 million pursuant to a Share Pledge Agreement dated 8 September 2017 (the "**Share**

[1] Ms Saunders is an employee of Watts/Frey's lawyers.

Pledge"). **[Saunders Affidavit, para 5 and Exhibit B]** The pledged shares of Country Way were deposited into escrow with Carlo V. Spadafora pursuant to an Escrow Agreement made as of 8 September 2017 (the "**Escrow Agreement**"). **[Affidavit of Laurel Saunders sworn 21 January 2021 ("Saunders Supp Affidavit'), Exhibit A]**

11. The SPA includes a provision whereby Watts/Frey agree to purchase the inventory and intangible assets of Country Way for the lesser of the amount owing on the $250K "down-payment" and the FMV of the assets. **[SPA Article 2.2(iv), Saunders Affidavit p18]**

12. The Share Pledge: (a) restricts the ability of 2595 Ontario to transfer, sell or (further) pledge the pledged shares of Country Way; and (b) provides Watts/Frey with the ability to vote the shares in a commercially reasonable manner in the event that 2595 Ontario defaults and Watts/Frey enforce their security over the shares. **[Share Pledge Article 4.01, Saunders Affidavit p 48]** There is no evidence that Watts/Frey ever exercised their rights under the Share Pledge.

13. The Escrow Agreement: (a) contemplates that the pledged shares will not be sold, transferred or (further) pledged; and (b) restricts how the pledges shares can be voted by 2595 Ontario. **[Escrow Agreement Articles 1.3 and 1.4, Saunders Supp Affidavit pp 3 and 4]**

14. On their face, the Share Pledge and Escrow Agreement apply to only the Class A Common Shares and the Class C Special Shares of Country Way.

15. In connection with the sale of the shares of Country Way to 2595 Ontario, Watts/Frey executed a Non-Competition Agreement (the "**Non-Compete**") in favour of Country Way and 2595 Ontario**. [SPA Exhibit E, Saunders Affidavit, pp 38-40]**

16. 2595 Ontario borrowed money from Country Way to pay Watts/Frey the obligations owing under the SPA. Country Way's business has been severely impacted by the COVID-19 pandemic. In 2020, the Debtor's gross monthly sales dropped by approximately 23% from pre-COVID levels. As a consequence, Country Way was unable to: (a) loan funds to 2595 Ontario to pay Watts/Frey; or (b) service its debt obligations and to pay its suppliers and employees. **[First Report of the Trustee dated 21 January 2022 ("Trustee Report"), para 4]**

17. In March of 2020, 2595 Ontario began to default on the monthly payments to Watts/Frey contemplated by the SPA. This resulted in Watts/Frey asserting that 2595 had repudiated the SPA. **[Saunders Affidavit, para 7]** On 21 January 2021, Watts/Frey commenced the Watts/Frey

Application against Ms Saari, who they assert was a party to the SPA in her personal capacity. The Watts/Frey Application was later amended to add 2595 Ontario as a Respondent. **[Saunders Affidavit, paras 9 and 13 and Exhibit C]** Country Way is not a respondent on the Watts/Frey Application.

18. On 3 May 2021, Country Way file the Proposal/Arrangement. **[Trustee Report, para 1]**

19. In addition to TNT, Royal Bank of Canada ("**RBC**") has registered a financing statement against the Debtor. Based on the Statement of Affairs, Country Way owes TNT about $192K and RBC about $69K. **[Saari Affidavit, para 18 and Trustee Report, para 16-18]**

20. Country Way is insolvent. **[Trustee Report, para 35]** The company owes creditors over $572K. It owes TNT $192K and RBC $69K. **[Trustee Report, para 17]** This exceeds the realizable value of Country Way's property. **[Trustee Report, paras 13, 15 and 34]**

21. Country Way developed the Proposal/Arrangement to address its insolvency for the benefit of its secured and unsecured creditors. The alternative to the Proposal/Arrangement is bankruptcy and the Trustee has determined that, in the event of a bankruptcy, Country Way's unsecured creditors will receive $0 and its secured creditors will suffer a significant deficiency. **[Trustee Report, paras 30-32]**

22. On 23 November 2021, Justice Hennessy of the Superior Court of Justice in Sault Ste. Marie heard the Watts/Frey Application via Zoom. Pursuant to a Decision on Application released on 22 December 2021 **[*Watts* v. *2595418 Ontario Inc.*, 2021 ONSC 8439 (CanLII)]**[2] Justice Hennessy found that 2595 Ontario had repudiated the SPA and that there was a breach by 2595 Ontario of the SPA such that Watts/Frey were entitled to the remedies provided to them under the SPA. His Honour ordered, among other things, declarations that:

1. 2595 Ontario has repudiated the SPA, which repudiation Watts/Frey accepted on or around 14 October 2020.

2. Watts/Frey are entitled to exercise all rights in the Debtor's shares, including voting rights.

[2] The decision has not yet been posted to CanLII.

3. Watts/Frey are entitled to acquire the inventory and tangible assets of the Debtor at a price of $0.

4. the on-going obligations of Watt/Frey under the Non-Compete have ceased.

23. The Proposal/Arrangement contemplates that: (a) the existing shares of Country Way will be converted to redeemable shares and redeemed for nominal consideration, which consideration reflects the current value of the equity in Country Way; (b) a new class of shares will be created and issued to Mr. Saari; and (c) Country Way will be amalgamated with 2655 Ontario and the common shares issued to Mr. Saari cancelled. **[Trustee Report, paras 24-29]** The ultimate effect of the Proposal/Arrangement is that the shareholders of 2655 Ontario will become the shareholders of the (amalgamated) company that owns the Country Way business.

24. 2655 Ontario is funding the costs of the Proposal/Arrangement. **[Saari Affidavit, para 24]** Those costs are estimated to be in excess of $50K **[Trustee Report, para 28]** The principal of 2655 Ontario is Ryan Saari, Ms Saari's spouse. **[Saunders Affidavit, para 14]**

25. The Trustee is not aware of any creditor of Country Way that opposes the Proposal. **[Trustee Report, para 20]**

26. Watts/Frey have, through counsel, asserted that they have "an interest of non-zero value in the shares" of Country Way, but have not explained to the Trustee how this can be the case given that Country Way is insolvent. Watts/Frey appear to attribute "value" to the shares based on the ability that it provides them to prevent Country Way from proceeding with the Proposal/Arrangement.

PART III – LAW AND ARGUMENT

A. The Proposal/Arrangement

27. The Proposal/Arrangement was validly filed by Country Way. As at 3 May 2021, the 22 Dec 21 Order had not yet been made and Watts/Frey had taken no steps to enforce their security in Country Way's shares. No resolution of shareholders or shareholder consent is required for an insolvent company to commence proceedings under Part III of the BIA. As noted further below,

in the absence of a unanimous shareholders agreement, shareholders have no direct right to control the business and affairs of a corporation.

B. Hearing of Arrangement and Proposal Together

28. The BIA contemplates that Part III may be applied together with s. 182 of the OBCA. **[BIA, s. 66(1.4)]** The BIA and the General Rules are, however, silent as to how the proceedings required by s. 182 of the OBCA are to be combined with proceedings under Part III when a debtor files a proposal that includes an arrangement.[3]

29. While the jurisdiction of the Superior Court and the Superior Court while sitting in bankruptcy and insolvency is not co-extensive, in circumstances where an arrangement is proposed pursuant to the OBCA as part of a proposal, there is justification for having the matters addressed together pursuant to the Court's jurisdiction under Rule 6.01 of the Rules of Civil Procedure. **[*Bankruptcy and Insolvency Act General Rules*, CRC. c. 368, Rule 3 and *Rules of Civil Procedure*, RRO 1990, Reg 194 ("Rules of Civil Procedure"), Rule 6.01]** The parties to the arrangement and the proposal are the same, the fundamental issues on an arrangement and a proposal are similar and tests applicable to the approval of an arrangement and a proposal are virtually identical. **[See *Legue* v. *Till-Fab Ltd.*, 2005 CanLII 63791 (ON SC), paras 12-13 and *Klassen* v. *Klassen*, 2020 ONSC 4835 (CanLII), paras 32-35]**

30. The Interim Order requested by 2655 Ontario is more-or-less "standard" in proceedings involving proposals involving insolvent companies that include arrangements and such orders are generally made on an unopposed basis. **[See, for example, *Eureka 93 Inc. (Re)*, 2020 ONSC 4415 (CanLII) and Order dated 16 July 2020]**

C. Watts/Frey's Motion

i. Transfer off the Commercial List

31. This Application was issued on the Commercial List on 30 April 2021.

[3] By way of contrast, there are no separate proceedings required where a debtor undertakes a corporate reorganization as part of a proposal.

32. Watts/Frey are requesting that this Application be transferred to the Superior Court in Sault Ste Marie so that it can be addressed at the same time and by the same Judge as is hearing the Watts/Frey Application as opposed to be addresses together with the Proposal.

33. There are no authorities cited by Watts/Frey in their Factum to support this request, but they appear to rely on Rules 6.01 and 13.1.02 of the Rules of Civil Procedure.

34. Rule 6.01 is applicable

(a) where the proceedings have a question of law or fact in common;

(b) the relief claimed in them arises out of the same transaction or occurrence or series of transactions or occurrences; or

(c) for any other reason an order ought to be made under this rule

35. There is no apparent overlap in the law of the (relevant) facts on this Application and the Watts/ Frey Application. The relief claimed on this Application and on the Watts/Frey Application does not arise out of the same transaction or occurrence or series of transactions or occurrences. And neither 2655 Ontario nor Country Way are parties to the Watts/Frey Application.

36. Watts/Frey brought their Motion prior to Justice Hennessy had heard the Watts/Frey Application. There is now nothing to be gained from a procedural perspective by having this Application heard with the Watts/Frey Application. At this point, it appears that the Watts/Frey Application seeks only a monetary Judgment against Ms. Saari. The remaining matters were addressed by the 22 Dec 21 Order. **[See *Watts* v. *2595418 Ontario Inc.*, 2021 ONSC 8438 (CanLII), paras 53-59]**

37. If Watts/Frey's Motion is granted and the Arrangement is transferred to the Superior Court in Sault Ste. Marie, the Arrangement/Proposal will have to be addressed separately by different Judges. The Arrangement is an integral part of the Proposal and the intention of s. 66(1.4) of the BIA is that the Proposal and the Arrangement will be addressed at the same time in a single forum.

38. While the Practice Directions, as noted by Watts/Frey, indicates that there should be a material connection to Toronto, there is discretion to list non-Toronto matters on the Commercial List. In this case, the Commercial List is the most logical and appropriate forum for the

Arrangement and the Proposal proceedings to heard and determined. The Commercial List Practice Direction contemplates that BIA and OBCA matters may be listed on the Commercial List and the Commercial List has developed a particular expertise in dealing with corporate arrangements and reorganizations.

39. The Proposal and the Arrangement proceedings have connections to Toronto aside from the presence of counsel. The Trustee is located in Toronto and a number of the creditors, including RBC, are located in Toronto. Aside from this Motion seeking an Interim Order, the only other matter to be dealt with by the Court in these proceedings will be the Motion **by the Trustee** seeking approval for the Proposal and the Arrangement. **[See OBCA, s. 182(5)(f) and BIA, s. 58(2)]**

40. In a remote environment where hearings can be conducted via Zoom using CaseLines or Sync, there is no prejudice to having that Arrangement and the Proposal deal with together on the Commercial List. It appears that matters before the Superior Court in Sault Ste. Marie are being dealt with remotely via Zoom. **[See Affidavit of Laurel Saunders sworn 21 January 2021, para 4]**

41. Rule 13.1.02(1) permits the Court, on its own initiative to transfer this Application to Sault Ste. Marie, it finds that the Application should have been commenced in Sault Ste. Marie and not Toronto. **[Rules of Civil Procedure, Rule 13.1.02(1)]** Subject to the Commercial List Practice Direction, this Application was properly issued in Toronto. Rule 13.1.01 appears to provide 2655 Ontario with the *prima facie* right to issue the Application in Toronto. **[Rules of Civil Procedure, Rule 13.1.01]**

42. Rule 13.1.02(2) permits Watts/Frey to ask to have the Application transferred to Sault Ste. Marie, but requires that they establish:

(a) that it is likely that a fair hearing cannot be held in the county where the proceeding was commenced; or

(b) that a transfer is desirable in the interest of justice, having regard to,

(i) where a substantial part of the events or omissions that gave rise to the claim occurred,

(ii) where a substantial part of the damages were sustained,

(iii) where the subject-matter of the proceeding is or was located,

(iv) any local community's interest in the subject-matter of the proceeding,

(v) the convenience of the parties, the witnesses and the court,

(vi) whether there are counterclaims, crossclaims, or third or subsequent party claims,

(vii) any advantages or disadvantages of a particular place with respect to securing the just, most expeditious and least expensive determination of the proceeding on its merits,

(viii) whether judges and court facilities are available at the other county, and

(ix) any other relevant matter. **[Rules of Civil Procedure, Rule 13.1.02(2)]**

43. The Factum filed by Watts/Frey provides no argument on these matters. However, there are no fairness issues that arise in having this Application determined in Toronto and none of the factors specifically enumerated in Rule 13.1.02(2)(b) favour having the Application determined in Sault Ste. Marie

ii. Request to be Added as Respondents

44. Watts/Frey are not creditors of Country Way. They are either secured creditors with a security interest in the shares of Country Way or shareholders of Country Way. It is not common for shareholders (or creditors) to be named as respondents to arrangement proceedings under the OBCA or proposal proceedings under the BIA.

45. There is no objection to appearing and making argument in opposition to the Arrangement and/or the Proposal. The law appears to be clear, however, that they have limited standing and cannot *qua* shareholders block the reorganization of Country Way.

iii. Adjournment of Request for Interim Order

46. There is no reason to adjourn the Motion by 2655 Ontario seeking an Interim Order.

47. Watts/Frey have been aware of the relief being requested by 2655 Ontario since at least May of 2021. **[Saunders Affidavit, para 17]** Watts/Frey delivered their Motion in June of 2021.

48. The meeting of Country Way's creditors to consider the Proposal was convened on 20 May 2021—within 21 days of the Proposal being filed, as required by the BIA. That meeting has been adjourned a number of times and cannot proceed until the Interim Order is made.

49. The Interim Order does not address the approval of the Proposal/Arrangement and there is no substantive impact on Watts/Frey's equity interest in Country Way that results from the Interim Order. Watts/Frey will have the opportunity to address the substantive impact the Proposal/Arrangement has on their equity interest when the Trustee brings the Motion seeking to have the Proposal/Arrangement approved pursuant to s. 58(2) of the BIA and s. 182(5)(f) of the OBCA.

D. Requested Interim Order

i. The Proposal/Arrangement

50. The BIA contemplates that Part III may be applied together with s. 182 of the OBCA. **[BIA, s. 66(1.4)]** The BIA and the Rules are, however, silent as to how the proceedings required by s. 182 of the OBCA are to be integrated with proceedings under Part III when a debtor files a proposal that includes an arrangement.[4]

51. The same practical effect as is accomplished by the Proposal/Arrangement could have been achieved by the sale of Country Way's property pursuant to s. 65.13 of the BIA or through a "liquidating" proposal, neither of which would have involved seeking the consent of Watts/Frey. **[See BIA, s 65.13(1)]** Those options would not, however, been as beneficial to Country Way's creditors as the Proposal/Arrangement.

52. It is not uncommon for the reorganization of an insolvency company to include a restructuring of the company's share capital, including the forced redemption/cancelation of shares, without the consent of shareholders: **[See, for example, *Canwest Global Communications Corp. (Re)*, 2010 ONSC 4209 (CanLII), para 7, *SkyLink Aviation Inc. (Re)*, 2013 ONSC 2519 (CanLII), para 20 and *Lydian International Limited (Re)*, 2020 ONSC 4006 (CanLII)]**

[4] There are no separate proceedings required where a debtor undertakes a corporate reorganization as part of a proposal.

53. The rationale for allowing such a reorganization is that the corporation is insolvent, which means that on liquidation the shareholders would get nothing. In those circumstances….. *there is nothing unfair or unreasonable in the court effecting changes in such situations without shareholder approval. Indeed, it would be unfair to the creditors and other stakeholders to permit the shareholders (whose interest has the lowest priority) to have any ability to block a reorganization.* **[See *Cable Satisfaction International Inc.* c. *Richter & Associés Inc.*, 2004 CanLII 28107 (QC CS), para 52 (translated by CanLII)]**

54. It is broadly accepted that shareholders cannot reasonably expect to maintain a financial interest in an insolvent company. **[*Canadian Airlines Corp (Re)*, 2000 ABQB 442 (CanLII), paras 74-79 and 143-145 leave to appeal ref'd, 2000 ABCA 238 (CanLII). See also *Cable Satisfaction International Inc.* c. *Richter & Associés Inc.*, 2004 CanLII 28107 (QC CS), para 52 and 53 (translation by CanLII) and *Forest* v. *Raymor Industries Inc.*, 2010 QCCA 578 (CanLII), para 4-6 (translation by CanLII)]**

55. In *Bouchard* v. *Industrial Turning and Tooling Company (SIDO) Ltd.*, the Quebec Superior Court found:

> *The jurisprudence has recognized that shareholders have no economic interest in the insolvent company, that they cannot defeat the proposal or arrangement contemplating the reorganization of the capital stock beneficial to the company and to all interested parties…* **[*Bouchard* v. *Industrial Turning and Tooling Company (SIDO) Ltd.*, 2010 QCCS 5997 (CanLII), paras 55-63 (translation by CanLII). See also *Peloton Pharmaceutiques Inc.*, 2017 QCCS 1165 (CanLII) (translation by CanLII)]**

56. As noted in *Unique Broadband Systems (Re)*:

> … shareholders who have no economic interest in a debtor should not be able to play with the creditors' money**….[*Unique Broadband Systems (Re)*, 2013 ONSC 676 (CanLII), para 54]**

ii. Right of Watts/Frey to Vote on Proposal/Arrangement

57. At the time the proposal was made, Country Way was an insolvent person within the meaning of the BIA and was entitled to file a proposal pursuant to Part III of the BIA. **[BIA, s. 50(1)]** Country Way satisfied all of the technical requirements to make a proposal. The BIA does not require shareholder approval to make a proposal.

58. There is no dispute that Watts/Frey are not entitled to vote on (or receive a distribution under) the Proposal. The issue is whether Watts/Frey should be entitled to vote on, and effectively veto, the Arrangement and thereby block the Proposal and bankrupt Country Way.

59. Whether or not the Proposal/Arrangement ought to be implemented based on the fact that it has the effect of forcing Watts/Frey to surrender their equity interest in County Way is not an issue that is to be determined at this time. Notwithstanding that they are not entitled to vote on the Arrangement to bring the approval of the Proposla/Arrangement into line with the approval of the Proposal, Watts/Frey are entitled to standing on the Motion **by the Trustee** seeking approval for the Proposal/Arrangement.

iii. Interim Order.

60. As a result of the Debtor being incorporated under the OBCA as opposed to the *Canada Business Corporations Act*, certain of the criteria applicable in a CBCA arrangement—the requirement that the change not be otherwise "practicable" and that the Debtor be solvent—are not applicable in this case. To obtain the Interim Order being requested, the Debtor must establish that:

(a) the fundamental change effected by the Proposal constitutes an "arrangement" within the meaning of s. 182(1) of the OBCA;

(b) the Director appointed under the OBCA has been given notice; and

(c) the Debtor is acting in good faith in putting forward the arrangement for approval. **[See *Concordia (Re)*, 2017 ONSC 6357 (CanLII), paras 24 and 25]**

61. **Proposal includes an Arrangement.** The reorganization of the debtor's capital structure is among the specific fundamental changes referenced in s. 182(1) of the OBCA.

62. **Director has been served.** The Director has been served with Application.

63. **Debtor acting in good faith.** The Debtor is, in the Trustee's view, acting in good faith in putting forward the arrangement for approval by its creditors.

64. There is nothing in the Proposal/Arrangement that is aimed at adversely impacting the economic interest of Watts/Frey as creditors of Ms Saari and/or 2595 Ontario—The effect of the Proposal/Arrangement is limited to Watts/Frey's interest as shareholders of Country Way based on having taken a pledge of the shares of the Country way—it does not include "third party" releases.

65. Watts/Frey argue that the Arrangement has not been put forward fro approval in good faith based on the assertion that: (a) the Arrangement is made with the intent to render ineffective Watts/Frey's security interest in the shares of Country Way and to frustrate their enforcement rights; (b) the Application was brought without any notice Watts/Frey; (c) the Arrangement offends the Share Pledge and the Escrow Agreement; and (b) there is no valid business purpose to the Arrangement.

66. The Arrangement does not adversely impact Watts/Frey's economic interest as the shareholders of Country Way. Through the 22 Dec 21 Order, Watts/Frey have effectively exercised their security over the shares of Country Way, but the shares have no realizable value as a result of the fact that Country Way is insolvent. Watts/Frey will receive $0 in a bankruptcy of Country Way. In that content, all that the Interim Order does is prevent Watts/Frey from exercising a veto over the reorganization of Country Way to force the company into bankruptcy.

67. Watts/Frey were not made respondents on the Application. Country Way was clear that Watts/Frey were not being given notice of the request for the Interim Order, but would receive a copy of the Proposal/Arrangement. **[Saari Affidavit, para 26]**

68. It is not clear how the Arrangement is prohibited by the Share Pledge or the Escrow Agreement. Moreover, in *Fiber Connections Inc.* v. *SVCM Capital Ltd.*, the Court found that a shareholder could not veto the alternation of the capital structure of an insolvent company reorganizing under Part III of the BIA. The case involved a proposal that contemplated an amendment to the debtor's share structure and that was, it appears, not permitted by a unanimous shareholders agreement. The Court found:

> *Where the corporation is insolvent and the shareholders would, upon liquidation, get nothing, it would be unfair to creditors and other stakeholders to permit one shareholder with no economic interest to block a reorganization. The alternative would be bankruptcy and nothing for most of the creditors and all of the shareholders.* **[*Fiber Connections Inc.* v. *SVCM Capital Ltd.*, 2005 CanLII 63760 (ON SC), paras 39 and 41-42]**

69. In terms of a valid business purpose, the Arrangement allows Country Way to: (a) secure financing to permit it to make the Proposal to its creditors by raising money based on the issuance of new shares; (b) simplify its capital structure; and (c) reduce RBC's unsecured claim by $20K. **[See Saari Affidavit, para 27]** The Proposal/Arrangement will preserve the employment of four (4) full-time and one (1) part-time employees. **[Saari Affidavit, para 21]**

70. There is no indication in the materials filed by Watts/Frey that they intend to themselves re-finance Country Way and fund a proposal to Country Way's creditors or otherwise address the claims of the company's secured and unsecured creditors in a way that will be satisfactory to the creditors.

71. Watts/Frey appear to assert that the approval by the Court of the Proposal/Arrangement is being addressed on its merits at this time. That is not correct. What is being requested is an Interim Order pursuant to s. 182(5) of the OBCA to 'marry-up" the Arrangement with Proposal so that the unsecured creditors can vote.

72. Assuming the Proposal/Arrangement is accepted, the Trustee will bring a Motion seeking approval under s. 59(2) of the BIA and s. 182(5)(f) of the OBCA,

73. In connection with the Arrangement, the Court will have to be satisfied that

(a) there has been compliance with the statutory and Court-ordered procedures;

(b) the application for approval has been put forward in good faith; and

(c) the arrangement is fair and reasonable**. [See *Canadian Real Estate Investment Trust (Re)*, 2018 ONSC 2519 (CanLII)]**

74. The test applicable to the approval of the Arrangement parallels the test applicable to the approval of the Proposal. **[See *Kitchener Frame Limited (Re)*, 2012 ONSC 234 (CanLII)]**

75. Watts/Frey should raise any arguments they have with respect to the impact of the Proposal/Arrangement of their equity interest in Country Way and whether the Arrangement was proposed in good faith on the Motion to approve the Proposal/Arrangement. Nothing in the Interim Order impacts their ability to oppose the Trustee's Motion seeking approval for the Proposal/Arrangement and the Trustee does not oppose Watts/Frey taking a position on that Motion that the Proposal/Arrangement ought not to be approved and the Debtor ought to be bankrupted.

E. Other Issues

76. There are issues that will have to be addressed should Watts/Frey wish to oppose the approval of the Proposal/Arrangement, but those issues are not directly relevant to the request that an Interim order be made to "marry-up" the Proposal under the BIA with the Arrangement under the OBCA.

i. Objective/Intent of Watts/Frey

77. The BIA does not permit the Debtor to withdraw the Proposal. **[BIA, s 50(4)]** As a result, the only option available to the Country Way is to make an assignment **[BIA, s. 50(4.1)]** or put the Proposal/Arrangement to a vote of the unsecured creditors**.**

78. The objective/intent of Watts/Frey appears to be to bankrupt Country Way, but they have not provided information with respect to their objective(s) in doing so and how the bankruptcy will benefit them *qua* shareholders of Country Way. There would, based on the Trustee's analysis as set forth in the Trustee Report, be no distribution to Country Ways shareholders. While they have not indicated an intention to do so, Watts/Frey have secured the release of the Non-Compete, which permits them to enter the market and compete with Country Way.

ii. Improper Purpose

79. The law appears to be clear that the Bankruptcy Court should not permit a person to exercise rights in a proposal proceeding to bankrupt a company for an improper purpose such as enhancing that person's own business interests. **[See *9354-9186 Québec Inc.* v. *Callidus Capital***

***Corp.*, 2020 SCC 10 (CanLII) and *Laserworks Computer Services Inc. (Bankruptcy) (Re)*, 1997 CanLII 1229 (NS SC) aff'd, 1998 NSCA 42 (CanLII)]**

iii. Control of Country Way

80. Under the OBCA, shareholders do not, in the absence of a unanimous shareholders agreement, have the direct right to manage Country Way's business and affairs. At best, Watt/Frey would have the right to remove and replace the director(s) of Country Way. Watts/Frey have not sought to do that and there I some doubt as to whether Watts/Frey could remove the director(s) for the purposes of terminating the Proposal/Arrangement and bankrupting the company. The BIA specifically addresses the removal of the directors of a company that has commenced proceedings under Part III and Watts/Frey have not brought a Motion under that provision. **[See BIA, s. 64. See also *Unique Broadband Systems (Re)*, 2011 ONSC 224 (CanLII)[5] and *FT ENE Canada Inc. (Re)*, 2019 ONSC 3969 (CanLII)[6]]**

iv. Right to Acquire Property for $0

81. Watts/Frey appear to have a contractual right to purchase such of the Debtor's property for $0. This appears to be inconsistent with the rights of Country Way's creditors and to be a contravention of the anti-deprivation rule. The effect of permitting Watts/Frey to acquire the Debtor's property for $0 has the direct effect of frustrating the scheme of the BIA. **[See *Chandos Construction Ltd.* v. *Deloitte Restructuring Inc.*, 2020 SCC 25 (CanLII) and *12178711 Canada Inc.* v *Wilks Brothers LLC*, 2020 ABCA 313 (CanLII), para 11]**

82. To the extent that Watts/Frey are entitled to purchase the Debtors' property for $0, they would acquire that property subject to the rights of RBC and TNT. **[*Personal Property Security Act*, RSO 1990, c. P.10, s. 25(1)(a)]**

v. Statutory Duty of Good Faith

83. Section 4.1 of the BIA requires that any interested person in a proceeding under the BIA act in good faith with respect to that proceeding. **[BIA, s. 4.1]** This provision has not been directly

[5] This decision has not been posted to CanLII. The CanLII citation is a duplicate.
[6] This decision has not been posted to CanLII.

considered in the context of proceedings under Part III of the BIA. The parallel provision in the CCAA was, however, considered in *9354-9186 Québec Inc.* v. *Callidus Capital Corp.* **[2020 SCC 10 (CanLII)]** where the Court found that the duty to act in good faith was relevant to considering whether a creditor should be barred from voting on a plan.

PART IV – RELIEF REQUESTED

84. The Trustee makes no formal request for relief, but, on the basis of what is in the best interest of Country Way's creditors: (a) supports the relief being sought by 2655 Ontario; and (b) opposing the relief being sought by Watts/Frey, subject to the condition that Watts/Frey can raise any issue they have with the Proposal/Arrangement on the Motion by the Trustee seeking approval from the Court for the Proposal/Arrangement.

ALL WHICH IS RESPECTFULLY SUBMITTED this 24th day of January 2022.

E. Patrick Shea

GOWLING WLG (CANADA) LLP
Barristers & Solicitors
1 First Canadian Place, Suite 1600
100 King Street West
Toronto, ON M5X 1G5

Lawyers for the Proposal Trustee

SCHEDULE A

Watts v *2595418 Ontario Inc.*, 2021 ONSC 8439 (CanLII)

Legue v. *Till-Fab Ltd.*, 2005 CanLII 63791 (ON SC)

Klassen v. *Klassen*, 2020 ONSC 4835 (CanLII)

Eureka 93 Inc. (Re), 2020 ONSC 4415 (CanLII)

Canwest Global Communications Corp. (Re), 2010 ONSC 4209 (CanLII)

SkyLink Aviation Inc. (Re), 2013 ONSC 2519 (CanLII)

Lydian International Limited (Re), 2020 ONSC 4006 (CanLII)

Cable Satisfaction International Inc. c. *Richter & Associés Inc.*, 2004 CanLII 28107 (QC CS)

Canadian Airlines Corp (Re), 2000 ABQB 442 (CanLII), leave to appeal ref'd, 2000 ABCA 238 (CanLII)

Forest v. *Raymor Industries Inc.*, 2010 QCCA 578 (CanLII)

Bouchard v. *Industrial Turning and Tooling Company (SIDO) Ltd.*, 2010 QCCS 5997 (CanLII)

Peloton Pharmaceutiques Inc., 2017 QCCS 1165 (CanLII)

Unique Broadband Systems (Re), 2013 ONSC 676 (CanLII)

Concordia (Re), 2017 ONSC 6357 (CanLII)

Fiber Connections Inc. v. *SVCM Capital Ltd.*, 2005 CanLII 63760 (ON SC)

Canadian Real Estate Investment Trust (Re), 2018 ONSC 2519 (CanLII)

Kitchener Frame Limited (Re), 2012 ONSC 234 (CanLII)

9354-9186 Québec Inc. v. *Callidus Capital Corp.*, 2020 SCC 10 (CanLII)

Laserworks Computer Services Inc. (Bankruptcy) (Re), 1997 CanLII 1229 (NS SC) aff'd, 1998 NSCA 42 (CanLII)

Unique Broadband Systems (Re), 2011 ONSC 224 (CanLII)

FT ENE Canada Inc. (Re), 2019 ONSC 3969 (CanLII)

Chandos Construction Ltd. v. *Deloitte Restructuring Inc.*, 2020 SCC 25 (CanLII)

12178711 Canada Inc. v. *Wilks Brothers LLC*, 2020 ABCA 313 (CanLII)

SCHEDULE B

***Bankruptcy and Insolvency Act,* RSC 1985, c B-3**

2 In this Act,

"equity claim" means a claim that is in respect of an equity interest, including a claim for, among others,

(a) a dividend or similar payment,

(b) a return of capital,

(c) a redemption or retraction obligation,

(d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or

(e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d);

"equity interest" means

(a) in the case of a corporation other than an income trust, a share in the corporation — or a warrant or option or another right to acquire a share in the corporation — other than one that is derived from a convertible debt, and

(b) in the case of an income trust, a unit in the income trust — or a warrant or option or another right to acquire a unit in the income trust — other than one that is derived from a convertible debt;

"insolvent person" means a person who is not bankrupt and who resides, carries on business or has property in Canada, whose liabilities 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;

4.2 (1) Any interested person in any proceedings under this Act shall act in good faith with respect to those proceedings.

(2) If the court is satisfied that an interested person fails to act in good faith, on application by any interested person, the court may make any order that it considers appropriate in the circumstances.

50 (1) Subject to subsection (1.1), a proposal may be made by

(a) an insolvent person;

…

(4) No proposal or any security, guarantee or suretyship tendered with the proposal may be withdrawn pending the decision of the creditors and the court.

(4.1) Subsection (4) shall not be construed as preventing an insolvent person in respect of whom a proposal has been made from subsequently making an assignment.

54 (2) For the purpose of subsection (1),

(a) the following creditors with proven claims are entitled to vote:

(i) all unsecured creditors, and

(ii) those secured creditors in respect of whose secured claims the proposal was made;

(b) the creditors shall vote by class, according to the class of their respective claims, and for that purpose

(i) all unsecured claims constitute one class, unless the proposal provides for more than one class of unsecured claim, and

(ii) the classes of secured claims shall be determined as provided by subsection 50(1.4);

(c) the votes of the secured creditors do not count for the purpose of this section, but are relevant only for the purpose of subsection 62(2); and

(d) the proposal is deemed to be accepted by the creditors if, and only if, all classes of unsecured creditors — other than, unless the court orders otherwise, a class of creditors having equity claims — vote for the acceptance of the proposal by a majority in number and two thirds in value of the unsecured creditors of each class present, personally or by proxy, at the meeting and voting on the resolution.

54.1 Despite paragraphs 54(2)(a) and (b), creditors having equity claims are to be in the same class of creditors in relation to those claims unless the court orders otherwise and may not, as members of that class, vote at any meeting unless the court orders otherwise.

58 (2) Where the court is of the opinion that the terms of the proposal are not reasonable or are not calculated to benefit the general body of creditors, the court shall refuse to approve the

proposal, and the court may refuse to approve the proposal whenever it is established that the debtor has committed any one of the offences mentioned in sections 198 to 200.

60 (1.7) No proposal that provides for the payment of an equity claim is to be approved by the court unless the proposal provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

(3) Where the proposal provides for the distribution of property in the nature of promissory notes or other evidence of obligations by or on behalf of the debtor or, when the debtor is a corporation, shares in the capital stock of the corporation, the property shall be dealt with in the manner prescribed in subsection (2) as nearly as may be.

64 (1) The court may, on the application of any person interested in the matter, make an order removing from office any director of a debtor in respect of whom a notice of intention has been filed under section 50.4 or a proposal has been filed under subsection 62(1) if the court is satisfied that the director is unreasonably impairing or is likely to unreasonably impair the possibility of a viable proposal being made in respect of the debtor or is acting or is likely to act inappropriately as a director in the circumstances.

(2) The court may, by order, fill any vacancy created under subsection (1).

65.13 (1) An insolvent person in respect of whom a notice of intention is filed under section 50.4 or a proposal is filed under subsection 62(1) 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) In the case of an individual who is carrying on a business, the court may authorize the sale or disposition only if the assets were acquired for or used in relation to the business.

(3) An insolvent person who applies to the court for an authorization shall give notice of the application to the secured creditors who are likely to be affected by the proposed sale or disposition.

(4) 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 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.

(5) If the proposed sale or disposition is to a person who is related to the insolvent person, the court may, after considering the factors referred to in subsection (4), 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 insolvent person; 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.

(6) For the purpose of subsection (5), a person who is related to the insolvent person includes

(a) a director or officer of the insolvent person;

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

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

(7) 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 insolvent person 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.

(8) The court may grant the authorization only if the court is satisfied that the insolvent person can and will make the payments that would have been required under paragraphs 60(1.3)(a) and (1.5)(a) if the court had approved the proposal.

(9) If, on the day on which a notice of intention is filed under section 50.4 or a copy of the proposal is filed under subsection 62(1), the insolvent person is a party to an agreement that grants to another party a right to use intellectual property that is included in a sale or disposition authorized under subsection (7), that sale or disposition does not affect the other party's right to use the intellectual property — including the other party's right to enforce an exclusive use — during the term of the agreement, including any period for which the other party extends the agreement as of right, as long as the other party continues to perform its obligations under the agreement in relation to the use of the intellectual property.

66 (1.4) The provisions of this Division may be applied together with the provisions of an Act of Parliament, or of the legislature of a province, that authorizes or provides for the sanction

of compromises or arrangements between a corporation and its shareholders or any class of its shareholders.

***Personal Property Security Act*, RSO 1990, c. P.10**

25 (1) Where collateral gives rise to proceeds, the security interest therein,

(a) continues as to the collateral, unless the secured party expressly or impliedly authorized the dealing with the collateral free of the security interest; and

(b) extends to the proceeds.

***Business Corporations Act*, RSO 1990, c. B.16**

115 (1) Subject to any unanimous shareholder agreement, the directors shall manage or supervise the management of the business and affairs of a corporation.

108 (3) Where a person who is the registered holder of all the issued shares of a corporation makes a written declaration that restricts in whole or in part the powers of the directors to manage or supervise the management of the business and affairs of a corporation, the declaration shall be deemed to be a unanimous shareholder agreement.

…

(5) A shareholder who is a party to a unanimous shareholder agreement has all the rights, powers, duties and liabilities of a director of a corporation, whether arising under this Act or otherwise, including any defences available to the directors, to which the agreement relates to the extent that the agreement restricts the discretion or powers of the directors to manage or supervise the management of the business and affairs of the corporation and the directors are relieved of their duties and liabilities, including any liabilities under section 131, to the same extent.

182 (1) In this section,

"arrangement", with respect to a corporation, includes,

(a) a reorganization of the shares of any class or series of the corporation or of the stated capital of any such class or series,

(b) the addition to or removal from the articles of the corporation of any provision that is permitted by this Act to be, or that is, set out in the articles or the change of any such provision,

(c) an amalgamation of the corporation with another corporation,

(d) an amalgamation of a body corporate with a corporation that results in an amalgamated corporation subject to this Act,

(e) a transfer of all or substantially all the property of the corporation to another body corporate in exchange for securities, money or other property of the body corporate,

(f) an exchange of securities of the corporation held by security holders for other securities, money or other property of the corporation or securities, money or other property of another body corporate that is not a take-over bid as defined in Part XX of the Securities Act,

(g) a liquidation or dissolution of the corporation,

(h) any other reorganization or scheme involving the business or affairs of the corporation or of any or all of the holders of its securities or of any options or rights to acquire any of its securities that is, at law, an arrangement, and

(i) any combination of the foregoing.

…

(5) The corporation may, at any time, apply to the court for advice and directions in connection with an arrangement or proposed arrangement and the court may make such order as it considers appropriate, including, without limiting the generality of the foregoing,

(a) an order determining the notice to be given to any interested person or dispensing with notice to any person;

(b) an order requiring a corporation to call, hold and conduct an additional meeting of, or to hold a separate vote of, all or any particular group of holders of any securities or warrants of the corporation in such manner as the court directs;

(c) an order permitting a shareholder to dissent under section 185 if the arrangement is adopted;

(d) an order appointing counsel, at the expense of the corporation, to represent the interests of shareholders;

(e) an order that the arrangement or proposed arrangement shall be deemed not to have been adopted by the shareholders of the corporation unless it has been approved by a specified majority that is greater than two-thirds of the votes cast at a meeting of the holders, or any particular group of holders, of securities or warrants of the corporation; and

(f) an order approving the arrangement as proposed by the corporation or as amended in any manner the court may direct, subject to compliance with such terms and conditions, if any, as the court thinks fit,

and to the extent that any such order is inconsistent with this section such order shall prevail.

***Bankruptcy and Insolvency General Rules*, CRC, c 368**

3 In cases not provided for in the Act or these Rules, the courts shall apply, within their respective jurisdictions, their ordinary procedure to the extent that that procedure is not inconsistent with the Act or these Rules.

***Rules of Civil Procedure*, RRO 1990, Reg 194**

1.04 (1) These rules shall be liberally construed to secure the just, most expeditious and least expensive determination of every civil proceeding on its merits.

6.01 (1) Where two or more proceedings are pending in the court and it appears to the court that,

(a) they have a question of law or fact in common;

(b) the relief claimed in them arises out of the same transaction or occurrence or series of transactions or occurrences; or

(c) for any other reason an order ought to be made under this rule,

the court may order that,

(d) the proceedings be consolidated, or heard at the same time or one immediately after the other; or

(e) any of the proceedings be,

(i) stayed until after the determination of any other of them, or

(ii) asserted by way of counterclaim in any other of them.

(2) In the order, the court may give such directions as are just to avoid unnecessary costs or delay and, for that purpose, the court may dispense with service of a notice of listing for trial and abridge the time for placing an action on the trial list.

13.1.02 (1) If subrule 13.1.01 (1) applies to a proceeding but a plaintiff or applicant commences it in another place, the court may, on its own initiative or on any party's motion, order that the proceeding be transferred to the county where it should have been commenced.

(2) If subrule (1) does not apply, the court may, on any party's motion, make an order to transfer the proceeding to a county other than the one where it was commenced, if the court is satisfied,

(a) that it is likely that a fair hearing cannot be held in the county where the proceeding was commenced; or

(b) that a transfer is desirable in the interest of justice, having regard to,

(i) where a substantial part of the events or omissions that gave rise to the claim occurred,

(ii) where a substantial part of the damages were sustained,

(iii) where the subject-matter of the proceeding is or was located,

(iv) any local community's interest in the subject-matter of the proceeding,

(v) the convenience of the parties, the witnesses and the court,

(vi) whether there are counterclaims, crossclaims, or third or subsequent party claims,

(vii) any advantages or disadvantages of a particular place with respect to securing the just, most expeditious and least expensive determination of the proceeding on its merits,

(viii) whether judges and court facilities are available at the other county, and

(ix) any other relevant matter.

(3) If an order has previously been made under subrule (2), any party may make a further motion, and in that case subrule (2) applies with necessary modifications.

Court No.: CV-21-00661436-00CL

IN THE MATTER OF SECTION 182 OF *THE BUSINESS CORPORATIONS ACT*, R.S.O. 1990, c. B.16, AS AMENDED AND IN THE MATTER OF A PROPOSED ARRANGEMENT OF 2655396 ONTARIO INC. AND INVOLVING 1776690 ONTARIO INC. COB COUNTRY WAY HEALTH FOOD STORE

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

FACTUM OF THE PROPOSAL TRUSTEE

GOWLING WLG (CANADA) LLP
Barristers and Solicitors
100 King Street West, Suite 1600
Toronto, ON M5X 1G5

E. Patrick Shea (LSO No.: 39655K)
Tel: (416) 369-7399 / Fax: (416) 862-7661
Email: patrick.shea@gowlingwlg.com

Lawyers for the Proposal Trustee

49193416\1