

The broader the better:

Review of expanding the CCAA stay of proceedings to third parties

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Introduction

The fundamental purpose of the *Companies' Creditors Arrangement Act* (“*CCAA*”)¹ is to allow an insolvent company the ability to carry on a business in the ordinary course while facilitating restructuring for the general benefit of its creditors.² Under the *CCAA*, courts have wide discretion to make orders providing the necessary court protection to allow the company breathing space to propose and implement its plan of arrangement. Under sections 11.02 and 11.03 of the *CCAA*, the court may make an order staying, restraining, or prohibiting any proceedings against the company or its directors. This stay of proceedings has been recognized as an imperative part of restructuring proceedings.³ Although the language of these sections provide a stay of proceedings against the company or its directors, the courts have expanded the scope of the stay and have applied it to third parties in circumstances where it is “just and reasonable” to do so.

The expansion of the stay of proceedings to third parties was established in *Lehndorff General Partner Ltd, Re*,⁴ and has been recently applied in the Montréal, Maine, and Atlantique (“*MMA*”), U.S. Steel Canada (“*USSC*”), and Target Canada Co. (“*Target*”) initial orders. This flexibility to expand the stay to third parties and fit the particular circumstances at hand is consistent with an underlying objective of the *CCAA* to maintain the status quo for the general benefit of the creditors.⁵ The stay expansion helps preserve the status quo, not only for the debtor company, but also for the ongoing business operations as a whole. This helps to provide the debtor company with the necessary space to maximize value for the general benefit of its creditors.

Recognizing the benefit to expanding the *CCAA* stay of proceedings to third parties

¹ R.S.C., 1985, c. C-36 [“*CCAA*”].

² See *Lehndorff General Partner Ltd., Re*, 1993 CarswellOnt 183, at para 5 (O.C.J. [Gen. Div. Commercial List]) [“*Lehndorff*”]; see also *Boutiques San Francisco Inc., Re*, 2004 CarswellQue 300 (Que. S.C.) at paras 16-18 [“*Boutiques*”] where the court stated at para 17: one of the main goals of the *CCAA* is to allow the debtor company seeking its protection to stay in business as a going concern while attempting to solve its financial difficulties. The Courts indeed recognize that the Act should be given a large and generous interpretation to favour this objective.

³ *Campeau v Olympia & York Developments Ltd.*, 1992 CarswellOnt 185 (O.C.J. [Gen. Div.]). In this case, a motion was brought before the court to lift the stay of proceedings afforded to the debtor company in order to allow the plaintiff to proceed with its action against the debtor company. The court dismissed the motion and continued the stay imposed under the *CCAA*. The court found that this did not prejudice the plaintiff since its action was not precluded, merely postponed. The court stated at para 17: To ensure the effective nature of such a “facilitative” process it is essential that the debtor company be afforded a respite from the litigious and other rights being exercised by creditors, while it attempts to carry on as a going concern and to negotiate an acceptable corporate restructuring arrangement with such creditors.

⁴ *Lehndorff*, *supra* note 2. In this case, the debtor company sought to extend the stay to its limited partnerships. The court analyzed the definition of “limited partnership” and the relationship of the limited partnerships with the debtor company. The court found that the business operations of the company and its limited partnerships were intertwined and creditors of the debtor company could look to the general partner’s interest in the limited partnership. The court held that the relief from the stay must therefore be extended to the limited partnerships as well.

⁵ *Boutiques*, *supra* note 2 at para 19.

One of the earliest cases discussing the court's ability to apply the stay to third parties was *Lehndorff*, where the court found that it had the inherent jurisdiction to extend the stay to the limited partnerships of the debtor. The court acknowledged its broad power under the *CCAA* to grant orders intended to prevent creditors from maneuvering their position to the prejudice of other creditors, thereby undermining the debtor company's financial position.⁶ The court found that although extending the stay to the limited partnerships would prejudice some non-creditors, this would be offset by the benefit it would provide to all creditors generally and to the restructuring company.⁷ With respect to its power to grant the requested order, the court held:⁸

The power to grant a stay of proceeding should be construed broadly in order to permit the *CCAA* to accomplish its legislative purpose and in particular to enable continuance of the company seeking *CCAA* protection. The power to grant a stay therefore extends to a stay which affected the position not only of the company's secured and unsecured creditors, but also all non-creditors and other parties who could potentially jeopardize the success of the plan and thereby the continuance of the company.

This passage emphasizes that the restructuring efforts of the debtor company for the benefit of its creditors generally is a central concern of the court when granting orders under the *CCAA*. The court looked at the broader goal of the restructuring and all of the circumstances of the particular case.

Recent application of expanding the *CCAA* stay of proceedings to third parties

Since *Lehndorff*, the stay of proceedings has continued to evolve to facilitate the orderly restructuring or winding-up of companies filing under the *CCAA* in a variety of circumstances. After the Lac-Mégantic rail disaster, the court in *MMA* was requested to make an initial order staying proceedings against XL Insurance, a non-related third party.⁹ Following and expanding on the principles articulated in *Lehndorff*, Castonguay J.C.S. stated that every case must be analyzed on its own merits and the decision must be based on the fair administration of justice.¹⁰ By filing for *CCAA* protection, *MMA* sought to channel all of the various claims and debt into an arrangement to submit to its creditors. In light of the multiple lawsuits already filed and those that

⁶ *Lehndorff*, *supra* note 2 at para 6.

⁷ *Ibid.*

⁸ *Ibid* at para 10.

⁹ 2013 QCCS 4039 [*MMA*]. In this case, a 74-car freight train carrying crude oil derailed, resulting in fires and explosions of multiple tank cars. The disaster destroyed approximately half of the downtown area of Lac-Mégantic, killing 42 people with 5 more missing and presumed to be dead. As a result of the disaster, numerous claims were filed against the railway company, *MMA*, and in August 2013, *MMA* filed for court protection under the *CCAA*. *MMA* sought to extend the stay of proceedings to include XL Insurance, its liability insurer. The novel issue which arose was whether a court would extend the stay to protect a solvent non-related third party company. Another interesting note is that the court had to consider whether the *CCAA* applied to *MMA*. Railways are excluded under *CCAA* s. 2, instead governed under the *Canada Transportation Act*, S.C. 1996, c. 10.

¹⁰ *Ibid* at para 65.

would be commenced, the court held that it would be in the fair interests of the administration of justice to extend the stay of proceedings to include XL Insurance.¹¹

In 2014, the extension of the stay to third parties was also sought in the USSC Initial Order. USSC wanted to ensure that two related entities, Baycoat and DC Chrome, were covered under the protection of the stay if an event of default or other rights or remedies were triggered by USSC's insolvency.¹² Both entities were critical to the delivery of certain finished steel products for existing USSC customers. If third parties were allowed to take advantage of the USSC insolvency, this would impact the business and property of USSC, jeopardizing delivery of certain products, and ultimately the restructuring process.¹³ The court agreed with the position taken by the applicant and sanctioned the broad stay in the initial order.¹⁴

Target's recent decision to utilize the *CCAA* to exit out of the Canadian market pushed the envelope of the scope of the stay of proceedings by including other Target corporate entities and landlords whom third party tenants may have a claim against arising from Target's insolvency.¹⁵ Target argued that a broad stay of proceedings was consistent with the purpose of the *CCAA* to give Target the breathing room necessary to facilitate the maximization of recoveries for the benefit of its creditors. Justice Morawetz exercised the court's broad jurisdiction to preserve the status quo in this situation to allow Target to maximize value while winding-down operations.¹⁶ He recognized the court's inherent jurisdiction to extend the protection of the stay to partnerships,¹⁷ and examined whether the court should extend the stay to rights of third party tenants against their landlords as a result of Target's insolvency. The court found that the landlords' claims against Target would significantly increase if the tenants were allowed to exercise their rights.¹⁸ Further, any prejudice to the third party tenants' creditors was found to be significantly outweighed by the benefits of the co-tenancy stay to all stakeholders of the Target entities.¹⁹ Finally, the court allowed the benefit of the stay to be extended to Target Corporation and its U.S. subsidiaries in relation to any derivative claims arising from the Target entities.

The approval of extending the stay to third parties demonstrates the court's willingness to use its inherent jurisdiction under the *CCAA* to assist debtor companies in their efforts to restructure. The commencement of litigation against a third party where liability and additional claims may ultimately fall on the filing company could be to the detriment of the restructuring process.

¹¹ This approach was endorsed in *4519922 Canada Inc., Re*, 2015 ONSC 124 [“*C&L*”].

¹² Factum of the Applicant USSC, Sept. 16, 2014, at para 44 [“*USSC Factum*”].

¹³ *Ibid* at para 45.

¹⁴ USSC Initial Order, Sept. 16, 2014, at para 18.

¹⁵ *Target Canada Co., Re*, 2015 ONSC 303 [“*Target*”]. Target sought a stay of proceedings to include: (1) the related partnerships of Target Canada Corporation; (2) Target Corporation and related entities for claims that are a derivative of the Target Canada entities; and (3) preventing third party tenants in commercial properties where Target stores or warehouses are located from asserting rights against their landlords that would arise as a result of Target's insolvency.

¹⁶ *Ibid* at para 50.

¹⁷ *Ibid* at para 42.

¹⁸ *Ibid* at para 45.

¹⁹ *Ibid* at para 46.

Likewise, the termination or refusal to perform contracts with related third parties due to the insolvency may impair the ongoing business operations of the restructuring company. Broad stay orders in the appropriate context helps maintain the status quo in order to afford the company the best possible chance to exit out of insolvency and maximize value for all stakeholders.

The *CCAA* was designed to afford mid to large sized companies the necessary court protection to undergo its required restructuring plan for the general benefit of its creditors.²⁰ Given the complex corporate structures created by mid to large sized, national and multi-national businesses today, a broad stay of proceedings that is extended to third parties is a necessary part of the tool-kit available to debtor companies. Often, the companies are so intertwined with various stakeholders that a successful restructuring requires the preservation of the status quo for the business as a whole, rather than just between the company and its creditors.²¹ Normally, a stay of proceedings extending to third parties that allows companies to continue ongoing business operations will preserve value for all stakeholders, which fundamentally furthers the purpose of the *CCAA*. It is important that the breathing space afforded by the stay is extended to the business undergoing the restructuring, rather than just the company that applies for protection. This enhances the chance of the development of a going-concern solution that maximizes value for all of the stakeholders.

Conclusion

The *CCAA* is to be liberally interpreted with the view that it should be a flexible restructuring tool. There is no better example of this than the courts' acceptance of a broad stay of proceedings granted in appropriate circumstances. The courts in the aforementioned cases recognized the crucial significance of the stay on the restructuring efforts of the filing companies and expanded the stay to third parties. This wide discretion is imperative for the Canadian insolvency regime, which benefits stakeholders as a collective whole. The contextual and discretionary tool afforded to the courts to expand the stay to third parties is consistent with the remedial goals of the *CCAA* and is a positive development in the evolution of insolvency law.

²⁰ See *CCAA*, *supra* note 1, s. 3. The *CCAA* only applies to corporations with a minimum debt of \$5,000,000.

²¹ For instance, see *Target*, where the corporate entities' business operations were so intertwined that the stay was necessarily afforded to the third party related corporate entities. See also *Lehndorff* and *USSC Factum*, discussed above.