Aquadis Case Comment: Extending the Reach of the Super Monitor

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Introduction –

The role played by the *CCAA* monitor in assisting the court as it shepherds along a corporate restructuring has evolved significantly over time. While still acting as the eyes of the court and standing apart from any particular stakeholder,[1] recent developments in insolvency law have seen the monitor take on an increasingly active part in proceedings. The decision of the Québec Court of Appeal in *Aquadis* affirmed another such expansion of the monitor's powers, as the Court approved a plan of arrangement that authorized the monitor to pursue the claims of the debtor's creditors against third parties within the *CCAA* proceedings.[2] Although the appellate court cautioned that exercising judicial discretion to grant such a power to the monitor is not to be done lightly,[3] ultimately this decision puts another tool into the insolvency practitioner's toolbox under the right conditions.

Background –

Aquadis International Inc. ("**Aquadis**") was a bathroom products importer and distributor, including for the sale of faucets. It acquired faucets from a Chinese distributor, Gearex, which had itself purchased them from the manufacturer, JYIC. Aquadis sold the faucets to various Québec retailers (the "**Retailers**") where they were purchased by consumers. The faucets were defective, resulting in many cases of water damage. Affected consumers made claims on their insurance policies and were subrogated by their insurers after payment.

The insurers constituted the majority of the creditor group. The aggregate value of the claims brought by the insurers against Aquadis exceeded its own insurance coverage, leading it

[1] See Luc Morin & Arad Mojtahedi, "In Search of a Purpose: The Rise of Super Monitors & Creditor-Driven *CCAA*s" in Jill Corraini and Blair Nixon (eds.), *Annual Review of Insolvency Law 2019* (Toronto: Thomson Reuters 2019), at 650.
[2] *Arrangement relatif à 9323-7055 Québec inc. (Aquadis International Inc.)*, 2020 QCCA 659 [*Aquadis #2*].
[3] *Ibid* at para 78 where Justice Schrager stated, "mere commercial expediency or good sense is not enough to qualify the exercise of judicial discretion under the *CCAA* as appropriate."

to file for *CCAA* protection. Raymond Chabot Inc. was appointed as monitor and granted the powers of the board of directors, who had resigned *en masse*. The monitor began negotiating with JYIC, Gearex, and the Retailers in an attempt to reach settlements involving full releases from liability in return for contributions to a litigation pool intended to satisfy the claims of the creditors. After concluding settlement discussions with several of Gearex and JYIC's insurers, the monitor filed a plan of arrangement (the "**Plan**") establishing the litigation pool and requesting the Québec Superior Court authorize the monitor to sue the Retailers on behalf of the creditors.[4] The Plan received unanimous approval from the creditors.

Judgment –

Superior Court of Québec

The *CCAA* judge approved the Plan over the objections of the opposing Retailers. The Retailers had challenged the Plan on the grounds that Aquadis had no right of action against them and that the rights of the creditors *vis-à-vis* the Retailers were unrelated to the Aquadis restructuring and therefore outside of the authority of the *CCAA*.[5] Justice Collier applied the three-part test from *AbitibiBowater*[6] in sanctioning the plan. He stated that the *CCAA*'s flexibility allowed it to adapt to the complex circumstances of the restructuring and empower the monitor to consolidate and represent all creditor claims in an effort to reach a global resolution of claims as the sole practical solution.[7] Citing Essar,[8] Justice Collier acknowledged that litigation was the only option to advance the restructuring given the lack of progress in settlement negotiations

[4] *Ibid* at para 26; *Arrangement relatif à 9323-7055 Québec inc.*, 2019 QCCS 5904 at paras 6 and 29 [*Aquadis #1*].
[5] *Aquadis #1, supra* note 4 at para 9.
[6] The three-part test from *AbitibiBowater Inc., Re*, 2010 QCCS 4450 at para 19 for exercise of a court's authority to sanction a *CCAA* arrangement is as follows: (a) there has been strict compliance with all statutory requirements; (b) nothing has been done or purported to be done that was not authorized by the *CCAA*; and (c) the Plan is fair and reasonable. Only the third requirement was in question in *Aquadis #1*.
[7] *Aquadis #1, supra* note 4 at paras 16-7 and 22.
[8] *Ernst & Young Inc. v Essar Global Fund Limited*, 2017 ONCA 1014 at para 123 [*Essar*].

with the Retailers over several years.[9]

Québec Court of Appeal

The Retailers appealed the decision, asking the Court to rule on whether a monitor appointed under the *CCAA* may be permitted to exercise the rights of creditors of the insolvent debtor to bring proceedings against third parties.[10] Writing for the Court unanimously, Justice Schrager dismissed the appeal and upheld the lower court's judgment. However, he did take the opportunity to further flesh out the legal basis supporting such a novel development in the law.[11]

The Court began by restating the fundamental principles underlying its power to grant additional powers to the monitor at its discretion.[12] While it recognized this discretion was not unlimited, it was appropriate to invoke it where consistent with the objectives of the *CCAA*,[13] which in the case at bar was maximizing creditor recovery as Aquadis had ceased operations. After canvassing the available case law and finding it of limited assistance due to the unique factual matrix present,[14] the Court discussed the Retailers' arguments. The Retailers claimed that permitting the monitor to exercise the rights of creditors would allow it to sue one group of creditors for the benefit of another group of creditors. Further, they argued such a move would violate the principle of the monitor's neutrality in the proceedings.

The Court disagreed, holding that the Retailers were not creditors[15] and regardless,

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[9] *Aquadis #1, supra* note 4 at para 29.
[10] *Aquadis #2, supra* note 2 at para 35. The Retailers also asked the Court to rule on a procedural issue regarding the timing of their challenge of the Plan of Arrangement given they had not objected to the initial order granting the Monitor the power to bring proceedings against them several years prior, but this ground of appeal is not relevant to this commentary and was dismissed without much discussion.
[11] *Ibid* at para 46.
[12] *Ibid* at para 61; *Companies' Creditors Arrangement Act*, RSC 1985, c C-36, s 23 [*CCAA*].
[13] *Aquadis #2, supra* note 2 at para 62.
[14] *Ibid* at paras 63-8.
[15] *Ibid* at para 71. The Retailers were not creditors, having declined to file claims in the proceedings and were identified as third parties by the Court. This eliminated any issue around collecting damages from one creditor to fund a litigation pool that would then pay some of those funds back to the same party.

amendments to the *CCAA* in 2007 to import certain powers of a bankruptcy trustee from the *Bankruptcy and Insolvency Act* meant that the concept of a monitor being empowered to enforce the rights of creditors was already contained in the framework of *CCAA* insolvency law.[16] The Court briefly disposed with the Retailers' argument on neutrality, stating that "as long as the monitor is objective and not biased and takes positions based on reasoned criteria to further legitimate *CCAA* purposes, … the neutrality it must maintain is attenuated."[17] In any case, as the Retailers were not creditors, it was unlikely the monitor had any obligation to them.[18] Justice Schrager acknowledged that "practical and equitable grounds" alone were not sufficient to ground exercise of judicial discretion to expand the monitor's powers. However, the unanimous vote of the creditors to permit the monitor to exercise their rights for them through the proposed action and litigation pool was the expression of the creditors' collective will and gave effect to creditor democracy under the *CCAA,* warranting such an expansion.[19]

Interestingly, the statutory basis the Court relied on to grant expanded powers to the monitor was section 23(k) of the *CCAA*, which directs that the monitor shall "carry out any other functions in relation to the company that the court may direct."[20] While the Retailers had argued that this new power was not "in relation to the company", the Court did not find this to be a barrier to the exercise of its discretion. The Court of Appeal's reasoning that *CCAA* section 23(k) could expand the monitor's powers to represent the debtor's creditors in a dispute unrelated to the debtor company was a significant move, potentially not in step with the wording of the provision.[21]

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[16] *Ibid* at para 70.
[17] *Ibid* at para 73; *Essar, supra* note 8 at paras 119-20.
[18] *Aquadis #2, supra* note 2 at para 74.
[19] *Aquadis #2, supra* note 2 at para 81; *CCAA, supra* note 12, s 6.
[20] *CCAA, supra* note 12, s 23(k).
[21] See Vern W DaRae & Alfonso Nocilla, "Bestriding the Narrow World: Is It Time to Bifurcate the Role of the *CCAA* Monitor?", in Janis Sarra (ed.), *Annual Review of Insolvency Law 2020* (Toronto: Thomson Reuters 2020) at

Discussion –

This decision pushes the boundaries of what powers a *CCAA* court may grant to a monitor in furtherance of pursuing a successful *CCAA* liquidation. As was noted in the judgment, empowering the monitor to pursue claims so as to establish a litigation pool with which to satisfy the claims of the debtor's creditors built on established precedent.[22] By taking it a step further than other courts, the Court in *Aquadis* facilitated the consolidation of what would have been a large number of claims into a single proceeding managed by the monitor.[23]

However, it is important to not overstate the impact of *Aquadis*. As the Court of Appeal held, the unique factual circumstances of *Aquadis*, both in the chain of distribution and in the number of claims being combined, justified departure from the general view that the *CCAA* should not be a vehicle to settle disputes other than between the debtor and its creditors.[24] The agreement of all creditors that their rights be exercised by the monitor had significant weight for the Court in determining there was a reasonable exercise of discretion in approving the Plan. Of further note was the Court's reference to the general acceptance of *CCAA* liquidations and "super monitors" where the situation warrants.[25] *CCAA* liquidations have been entrenched in the legal landscape as a necessary process to accommodate diverse restructuring outcomes and such undertakings naturally focus courts on the maximization of creditor recovery, providing an

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224 where the authors suggest that the Court in *Aquadis* may have better grounded its decision in its equitable and inherent jurisdiction or under *CCAA* section 11.

[22] See *Muscletech Research and Development Inc. (Re)*, 2007 CanLII 5146, a similar product liability *CCAA* case with a plan of arrangement involving liability releases provided by the monitor in exchange for contributions to a litigation pool and *Sino-Forest Corporation (Re)*, Court file No CV-12-9667-00CL, December 3, 2012 Ontario Superior Court of Justice, a *CCAA* case involving a litigation trust that included rights of action against third parties.

[23] *Aquadis #2, supra* note 2 at para 67.

[24] See *Pacific Coastal Airlines Ltd v Air Canada*, 2001 BCSC 1721 at para 24; see especially *Urbancorp Cumberland 2 GP Inc., (Re)*, 2017 ONSC 7649 at paras 20-2 where the court refused to permit the monitor to claw back a payment from one creditor on behalf of the others [*Urbancorp*].

[25] *Aquadis #2, supra* note 2 at 68; see also Morin & Mojtahedi*, supra* note 1 where the authors acknowledge that resignation of management is a key aspect defining a body of *CCAA* liquidations involving super monitors.

opening for increased monitor engagement.[26]

It is clear that the *CCAA* framework is becoming increasingly friendly to an expanded role for the monitor,[27] however this gradual drift to active monitor participation has serious implications for insolvency proceedings. There is a risk of damaging the neutral status of the monitor as the impartial officer of the court if it may take an adversarial position against certain parties in an insolvency.[28] This setting should be considered when examining the court's willingness to approve novel strategies to ensure maximization of funds to satisfy creditor claims. While the Court of Appeal cautioned that predictability must continue to govern the exercise of judicial discretion,[29] the broad recognition of *CCAA* liquidations and the rise of the "super monitor" have opened the door for restructurings to make significant strides in what is permissible.

Aquadis illustrates that in the pursuit of fulfilling the purposes of the *CCAA*, the court may be convinced to approve monitor powers that stray from traditional framework of a debtor-and-creditor dispute resolution statute. Justice Myers observation in *Urbancorp* remains an instructive starting point for future *CCAA* courts to consider before handing expanded powers involving creditors' rights to a monitor: "why is this a fight for the Monitor rather than the creditors who stand to benefit from the claim?"[30]

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[26] *9354-9185 Québec inc. v Callidus Capital Corp.*, 2020 SCC 10 at paras 42-5.
[27] See Julie Himo & Arad Mojtahedi, "The Evolving Role of the Eyes and Ears of the Court: Empowering the *CCAA* Monitor to Initiate Legal Proceedings Against Third Parties" in Janis Sarra (ed.), *Annual Review of Insolvency Law 2020* (Toronto: Thomson Reuters 2020), at 120 for an overview of the trend towards monitors as active participants in *CCAA* proceedings; see also DaRae & Nocilla*, supra* note 21 for a more in depth discussion of the same.
[28] See *Century Services Inc. v Canada (Attorney General)*, 2010 SCC 60 at para 70 where the Supreme Court stated that *CCAA* courts should treat all stakeholders as advantageously and fairly as the circumstances permit. While the Court of Appeal in *Aquadis* saw the Retailers as third parties (not stakeholders), there was little discussion of the reasons for that factual finding.
[29] *Aquadis #2, supra* note 2 at para 78.
[30] *Urbancorp, supra* note 24 at para 21.