Court File No. 05-CL-5801
Date: 20050323

ONTARIO
SUPERIOR COURT OF JUSTICE

IN THE MATTER OF: *THE COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED	*Justin R. Fogarty, Renée B. Brosseau,* for the Applicants
AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF: THE MANDERLEY CORPORATION, 1310500 ONTARIO INC. and LEO BEAL LTD.	*Clifton Prophet, Massimo C. Starnino,* for the Royal Bank of Canada
Applicants	**Heard**: March 18, 2005

C. CAMPBELL J.:

REASONS FOR DECISION

Background

[1] The Applicants seek orders permitting the continuance of proceedings commenced by them uner Part III of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "BIA") and relief under the *Companies' Creditors Arrangement Act* (the "CCAA") for the appointment of a monitor, an interim receiver and authorization of debtor in possession ("DIP") financing.

[2] The relief sought is opposed by Royal Bank of Canada ("RBC"), who seeks to appoint its agent as interim receiver and receiver of the property of the Applicants essentially for the purpose of liquidation.

[3] Manderley and its subsidiaries are family-held Ontario corporations, which together are one of the largest turf grass producers in North America, with over 81,000 acres of production across Canada and clients in national and international markets.

[4] Manderley is insolvent, with RBC being its largest secured creditor, owed in excess of $3,600,000 at the present time, out of a total of $16.5 million known liabilities, both secured and unsecured.

[5] The indebtedness of Manderley to RBC involved (a) term loan of $4 million; (b) a revolving term facility of $250,000; and (c) a corporate Visa account minimum of $200,000, secured by a general security agreement over all company's assets and personal guarantees of the principals.

[6] As a result of financial problems said to be due in large part to the rise in the Canadian dollar as against the United States dollar, Manderley was unable to satisfy RBC in respect of its obligations.

[7] As a result, Manderley entered into a Forbearance Agreement with RBC, whereby there was a reduction in the line of credit with the sale of what is called the Brantford Farm and application of its proceeds.

[8] On March 2, 2005, RBC advised that the company was in default of its obligations under the Forbearance Agreement and made a demand for payment of $3,606,612.23 and delivered notice of intention to enforce. This Application was made on March 14, 2005 under s. 47.1 of the BIA and s. 11 of the CCAA for the relief referred to above.

Position of the Applicants

[9] The Applicants propose what has come to be called a "two track approach." The first is the appointment of a Proposal Trustee under the BIA and the second the appointment of the same entity (Doyle Salewski Inc.) as an interim receiver and monitor under the CCAA. In addition, the Applicants request the authorization of DIP financing for the purposes of re-organization. Such financing to be in priority to secured creditors without their consent. These would include RBC.

[10] The position of the Applicants is that they are to develop a restructuring plan that will (i) provide full repayment to RBC and possibly the other secured creditors; (ii) likely produce a dividend to unsecured creditors; (iii) preserve jobs; and (iv) keep the business moving going forward to maintain growing operations to be able to realize on the inventory currently planted.

[11] It is the position of the Applicants that RBC has failed to provide any reasonable argument to substantiate how the CCAA process and the interim receiver and monitor appointments cause them any further prejudice than any other financial institution in the same situation. In other words, it is submitted there is nothing unique in RBC's position and in fact, their position is unremarkable.

Position of RBC

[12] The position of RBC is contained in its motion record, which seeks the appointment of Raymond Chabot Grant Thornton Limited ("Grant Thornton") as interim receiver of Manderley for the purpose of controlling receipts and disbursements.

[13] The motion of RBC is supported by the affidavit of Stanley Loiselle, a partner of Grant Thornton, who has been retained by RBC to assess the Bank's security portion. Mr. Loiselle's affidavit was filed in response to the affidavit of Christopher Hope of Manderley, and in essence disagrees with the proposition that the CCAA process has any chance of working.

[14] Purporting to speak as agent for the RBC, Mr. Loiselle concludes that a 30-day stay under the BIA should only be permitted in order to allow Manderley to arrange takeout financing but based on the Bank's lack of confidence in Manderley, it opposes the conversion of the

bankruptcy to CCAA proceedings or support or restructuring process, believing that orderly realization of the Company's property and assets should be undertaken in the proposed receivership.

Issue

[15] The question for determination on these motions is whether on the facts before the Court, it is appropriate to grant CCAA relief by permitting a monitor to arrange DIP financing for either a restructuring or orderly liquidation, as opposed to the appointment of a Receiver for the express purpose of immediate realization of assets to ensure preservation of security.

Law & Analysis

[16] The basic premise on which RBC seeks its relief is that it has lost confidence in management to arrange a restructuring and based on that lack of confidence, believes orderly liquidation is the only means of preserving its security. RBC, through its agent Grant Thornton, believes that the Bank's security and the ability to recover its full debt owed will be impaired if DIP financing is allowed to take priority.

[17] Counsel for Manderley urges that the structure of the DIP financing and the bi-weekly reporting about it, together with a reporting schedule that is premised on performance, will not impair RBC's security. Further, it is submitted there is the possibility (albeit small) of recovery of the Company but at the very least, the CCAA process will permit an orderly and market-driven sale of sod inventory, which will maximize return for all creditors, not just RBC.

[18] The operative legal principles are set out in the following quotations from Houlden & Morawetz' *Bankruptcy & Insolvency Analysis* (Carswell, 2004), section N16 – Stay of Proceedsings – 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.
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> 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: *United Used Auto & Truck Parts Ltd., Re* (1999), 12 C.B.R. (4th) 144, 1999 CarswellBC 2673, [1999] B.C.J. No. 2754 (B.C. S.C. [In Chambers]); affirmed 2000 BCCA 146, 73 B.C.L.R. (3d) 236, [2000] 5 W.W.R. 178, 16 C.B.R. (4th) 141, 135 B.C.A.C. 96, 221 W.A.C. 96, 2000 CarswellBC 414, [2000] B.C.J. No. 409 (B.C. C.A.); leave to appeal granted (2000), 261 N.R. 196 (note), 149 B.C.A.C. 160 (note), 244 W.A.C. 160 (note), 2000 CarswellBC 2132, 2000 CarswellBC 2133, [2000] S.C.C.A. No. 142 (S.C.C.), but appeal dismissed. See the very helpful case comment by Michael B. Rotsztain 12 C.B.R. (4th) 156.
>
> 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: *United Used Auto & Truck Parts Ltd., Re, supra.*

[19] In *Re Skydome Corp.,* (1998) CarswellOnt 5922 (Ont. Gen Div.); 16 C.B.R. (4th) 118, 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. See also *Re Lehndorff General Partner Ltd.* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]); *Olympia & York Developments Ltd. v. Royal Trust Co.* (1993), 17 C.B.R. (3d) 1 (Ont. Gen. Div.).

[20] These comments were adopted by Farley J. in *Royal Oak Mines Inc. (Re),* [1999] OJ No. 864 (Ont.Gen.Div.) In that case, the specific finding was that the CCAA court did not have jurisdiction to grant super-priority over builders' liens. Nevertheless, the above passage from Blair J. in *Re Skydome* was adopted and super-priority granted apart from that issue.

[21] Immediately following the quotation from *Skydome,* Farley J. went on to say at paragraph 22 of *Royal Oak*:

> Implicit in his analysis and part of the equation is the reasonably anticipated benefits for all concerned which derive from these sacrifices. It would seem to me that Holden J.A. in his endorsement in *Re Dylex Limited* released January 23, 1995 implicitly engaged in this balancing of prejudices act where he observed:
>
> > I do not believe that the Bank of Montreal will be adversely affected by the making of this order. As a result of the bridge financing, new receivables will be generated which will assist in re-paying or securing the bridge financing.
>
> Better and more timely information will be of assistance in minimizing the momentum effect in the future. My conclusion as to the appropriateness of the superpriority granted the DIP financing is of course limited to the Initial Order $8.4 million amount and is based upon the conditions now determined to be prevailing as of the authorization date. Each subsequent DIP financing authorization and the priority to be attributed to it will have to be determined on the merits and circumstances then existing.

[22] I am of the view that these comments are applicable to the facts of this case.

[23] I have read the first report of the Proposal Trustee, the proposed financing Term Sheet, together with the cash flow forecast – assuming orderly liquidation.

[24] As against this, there is the affidavit evidence of Mr. Loiselle, which essentially proffers the opinion that Manderley will not survive restructuring and since the Bank has lost confidence in management, the liquidation should be hastened rather than delayed.

[25] I am satisfied on the evidence before me that, at least for the next 30 days, the benefits of the proposed financing clearly outweigh the prejudice to RBC, the opposing creditor.

[26] I reach this conclusion for the following reasons:

a) the limitation on the drawdown of the proposed financing, the "Drip DIP" as it was called, to $250,000 within the next week to 10 days, instead of the entire proposed $418,000 in one tranche;

b) the lack of independent analysis by RBC as to why its security would realistically be at risk over the next two weeks;

c) it would appear on the evidence before me that Mr. Loiselle did not place any value on the equipment evaluation of Manderley since some of that was secured. While I recognize that the values may not be accurate or up-to-date, nevertheless they do establish some significant net value after taking security into account.

[27] Applying the balancing act that is the hallmark of DIP financing in this kind of a situation, that balance at least for the next 30 days provides the opportunity to potentially bring greater value to the enterprise as a whole than would be the case if the RBC plan were accepted.

[28] Having reached this conclusion, I am satisfied it is reasonable to allow the proposed Proposal Trustee to be approved, to permit the 30-day stay sought on the terms and conditions proposed in the draft order, including the right of RBC or any other creditor to return to Court on short notice if need be. The Applicants shall also for the same period be permitted to restructure under the proposed CCAA plan of compromise or arrangement set out in the draft order and plan.

[29] Doyle Salewski Inc. is hereby appointed monitor of the business and affairs of the Applicants on the terms as set out in the draft order, subject to any revision that may become necessary as a result of the terms of these reasons. The DIP financing proposal is approved, again subject to the terms of the draft order but subject to such revisions as may be required as a result of submissions made by counsel and these reasons.

[30] The motion made by RBC for the appointment of Grant Thornton is dismissed, but without prejudice to its renewal on the first come-back date if circumstances should change, such as to make a compelling case as to the risk to its security of the continuance of the CCAA plan. I am satisfied that for the 30 day period of the stay, a preferable receiver to Grant Thornton is one who is open to other considerations than immediate liquidation.

[31] During the course of argument there were submissions as to the appropriateness of an order making some of the financial information that would be crucial to remain confidential for the Plan to be successful. If counsel can agree on these items, I may be advised in writing. If there is disagreement on this issue or the form of order that may follow from these reasons, I may be contacted for an in-person or telephone conference call.

[32] If it is necessary to deal with the issue of costs, written submissions should be received within the next 10 days.

Released: March 23, 2005

C. CAMPBELL J.

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