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COURT FILE NO.:	25-2332583 25-2332610 25-2335351
COURT	COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
PROCEEDINGS	IN THE MATTER OF THE NOTICE OF INTENTION TO MAKE A PROPOSAL OF MANITOK ENERGY INC. IN THE MATTER OS THE NOTICE OF INTENTION TO MAKE A PROPOSAL OF RAIMONT ENERGY CORP. IN THE MATTER OF THE NOTICE OF INTENTION TO MAKE A PROPOSAL OF CORINTHIAN OIL CORP.
DOCUMENT	**BOOK OF AUTHORITIES**
PARTY FILING THIS DOCUMENT	**YANGARRA RESOURCES LIMITED**

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT

McMillan LLP
#1700, 421 – 7th Avenue SW
Calgary, AB T2P 4K9

Attention: Andrew E. Stead
Phone: 403.531.4700
Fax: 403.531.4720
Matter No. 269125

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IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, as amended

IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF DENNINGHOUSE INC. AND THE OTHER COMPANIES LISTED IN SCHEDULE "A" (Applicants)

EXTREME RETAIL (CANADA) INC. and BUCK OR TWO (2004) INC. (Moving Parties) v. BANK OF MONTREAL (Responding Parties)

Stinson J.

Heard: August 3, 2007
Judgment: September 5, 2007
Docket: 04-CL-005523

Counsel: Robert C. Harason for Moving Parties
Harvey G. Chaiton for Responding Parties

Subject: Insolvency; Corporate and Commercial

Related Abridgment Classifications

Bankruptcy and insolvency
XIX Companies' Creditors Arrangement Act
XIX.3 Arrangements
XIX.3.d Effect of arrangement
XIX.3.d.i General principles

Headnote

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Arrangements — Effect of arrangement — General principles

ABOT Inc. had general security agreements ("GSAs") over assets of its franchises — Bank also had GSAs with seven of franchises that were perfected later in time — ABOT Inc.'s parent company had subordination agreement with bank but ABOT Inc. itself never made such agreement — Parent company obtained CCAA protection — Company sold franchise agreements and ABOT Inc.'s GSAs to purchaser pursuant to approval and vesting order — Order provided that assets were free and clear of any security interests or other rights — Purchaser brought motion for declaration that its GSAs had priority over bank's GSAs — Motion granted — Order was clear and superseded any priority bank may have had over ABOT Inc. — Bank was party to proceedings and failed to claim priority at that time — Matters resolved by order were res judicata.

Table of Authorities

Cases considered by *Stinson J.*:

Air Canada Pilots Assn. v. Air Canada Ace Aviation Holdings Inc. (2007), 2007 CarswellOnt 123, 28 C.B.R. (5th) 163, 57 C.C.P.B. 204, 26 B.L.R. (4th) 124 (Ont. S.C.J.) — followed

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Rules considered:

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MOTION by purchaser of assets pursuant to approval and vesting order under *Companies' Creditors Arrangement Act* for declaration of priority of its security agreements.

***Stinson J.*:**

1 This motion involves a dispute concerning the effect of a vesting order made in connection with the sale of certain assets during the course of this CCAA proceeding.

2 Prior to this CCAA proceeding, Denninghouse Inc. and its subsidiaries (the "Denninghouse Group") were in the business of operating a cross-Canada chain of discount retail stores or so-called dollar stores, principally under the name of "A Buck or Two" stores. The principal lender to Denninghouse Group was the Bank of Montreal ("BMO").

3 Most of the "Buck or Two" stores were operated by franchisees, pursuant to franchise agreements between ABOT Franchise Inc. ("ABOT") as franchisor and the individual store operators as franchisees. ABOT was a subsidiary of Denninghouse Inc. Among other things, ABOT supplied inventory to the franchisees on credit terms. To secure its position, ABOT sought and received general security agreements ("GSAs") over the franchisees' assets (the "ABOT GSAs").

4 In addition to providing financing to the Denninghouse Group, BMO also provided financing directly to individual "Buck or Two" franchisees, pursuant to a franchisee financing plan arranged with BMO by representatives of Denninghouse Group. Pursuant to that plan, BMO also was to receive GSAs from the franchisees, in order to secure its lending to them (the "BMO GSAs"). Also as part of the plan, Denninghouse Inc. (the parent company) provided to BMO two signed agreements in relation to each franchisee financed by BMO, being a Letter of Comfort and Inventory Buy-Back Agreement, and a Subordination Agreement.

5 Significantly, although ABOT was the corporation that had the direct franchisor-franchisee relationship with the franchisees, the Letters of Comfort and Inventory Buy-Back Agreements and the Subordination Agreements were in the name of and signed by Denninghouse Inc. alone. In those documents, Denninghouse Inc. agreed to postpone to BMO's security, all security or other interests that it had over the franchisees or their property. Moreover, in the Subordination Agreements, Denninghouse Inc. agreed to cause its subsidiaries (which included ABOT) to subordinate their rights against the assets of the franchisees, to the rights of BMO. As events unfolded, however, Denninghouse Inc. never caused ABOT to do so and no separate Letters of Comfort and Inventory Buy Back Agreements or Subordination Agreements were ever executed by ABOT in favour of BMO.

6 ABOT registered the ABOT GSAs under the relevant *Personal Property Security Act* ("PPSA") regimes in the provinces in which the franchisees' stores were located. BMO did the same. In a total of seven instances, ABOT's PPSA registrations for the ABOT GSAs of particular franchisees pre-dated those of the BMO GSAs for the same franchisees.

7 On August 16, 2004, the Denninghouse Group sought and obtained an order declaring themselves subject to the CCAA ("the Initial Order"). BMO was among the parties represented in court when the Initial Order was made. The Initial Order appointed RSM Richter Inc. to act as Monitor.

8 Following the Initial Order, proposals were sought for the purchase of various of the assets of the Denninghouse Group, including the franchise agreements and the ABOT GSAs. In due course, the Monitor and the Denninghouse Group entered into an agreement of purchase and sale with the moving parties, Extreme Retail (Canada) Inc. and Buck or Two (2004) Inc. ("Extreme"). The sale to Extreme was approved by the court and implemented by means of an order dated December 7, 2004 (the "Approval and Vesting Order"). Extreme paid the consideration contemplated by the agreement of purchase and sale and, pursuant to the Approval and Vesting Order, became the owner of the assets, including the franchise agreements and the ABOT GSAs.

9 Significantly, BMO was one of the parties represented in court when the Approval and Vesting Order was granted.

10 The operative provision of the Approval and Vesting Order that effected the conveyance and transfer of ownership to Extreme, provided that the assets (including the ABOT GSAs) "... are vested in Extreme ... absolutely and forever, free and clear of and from any and all right, title and interest of the applicants [the Denninghouse Group] and of any, security interests, charges, pledges, mortgages, ... adverse claims, ... disputes, ... limitations or restrictions, ... charges, encumbrances, or any other rights, ... whether contractual, statutory, by operation of law or otherwise, whether secured, unsecured or otherwise ...."

11 In addition, as part of the closing of the sale transaction, BMO provided to Extreme a comfort letter dated December 10, 2004, that provided as follows:

> ... please accept this letter as confirmation that [BMO] hereby waives any rights it may have to pursue [Extreme] for enforcement and collection of any monies arising from and pursuant to the terms of any inventory buy-back agreements, guarantees or security provided by and executed in favour of [BMO] by the Denninghouse Group given in respect of any indebtedness of a franchisee.

12 In 2006, well after the sale and the Approval and Vesting Order, two Buck or Two franchisees in the Province of Alberta encountered financial problems. Their assets were liquidated. A dispute then arose between Extreme and BMO as to which of them was entitled to priority over the proceeds of realization. The franchise agreements and ABOT GSAs for those franchisees were part of the assets purchased by Extreme from ABOT. BMO also held BMO GSAs in relation to the assets of these franchisees. The PPSA registrations of the BMO GSAs, however, were subsequent to the registrations of the ABOT GSAs. Both franchisees were indebted to each of Extreme and BMO. By agreement of the parties, the funds have been held in trust, to be released by agreement or by court determination as to which of Extreme or BMO is entitled thereto.

13 In addition to their dispute concerning the proceeds of realization of the two Alberta franchisees mentioned above, the parties have determined that there are five other franchisee relationships, some in Alberta and some in Ontario, in relation to which the ABOT GSAs in relation to those franchisees were registered under the relevant PPSA regime prior to the registration of the BMO GSAs for the same franchisees. Extreme has therefore asked the court to declare the rights of the parties in relation to those franchisee GSAs, as well as in relation to the proceeds of realization that remain held in trust.

14 Extreme claims priority over the position of BMO by reason of the fact that the ABOT GSAs acquired by it pursuant to the Approval and Vesting Order were registered in priority to the BMO GSAs given by the franchisees to BMO. Extreme argues that ABOT never agreed to subordinate its position nor did it enter into any Subordination Agreements with BMO. Extreme further argues that it acquired the GSAs free and clear of any prior rights, pursuant to the Approval and Vesting Order. Finally, Extreme argues that the comfort letter signed by BMO as part of the sale transaction precludes BMO from disputing Extreme's priority.

15 BMO argues that the agreements signed by Denninghouse Inc. with BMO bound ABOT, since Denninghouse Inc. was the 100 percent shareholder of ABOT. BMO further argues that Denninghouse Inc. signed the Subordination Agreements on behalf of ABOT as its agent. In the alternative, BMO asserts that there was an oral subordination agreement between ABOT and BMO. The end result, asserts BMO, is that the ABOT GSAs acquired by Extreme rank in priority after the BMO GSAs, despite their prior registrations under the relevant PPSAs. BMO further argues that the Approval and Vesting Order was never intended to deprive BMO of its priority in relation to the BMO GSAs obtained by it in exchange for financing the franchisees, which was a separate lending arrangement, independent of the financing provided by BMO to the Denninghouse Group. Those arrangements, BMO agrees, were not intended to be affected by the CCAA proceedings, or the Approval and Vesting Order. Lastly, BMO argues that the December 10, 2004 comfort letter provided by it was also not intended to waive any of BMO's rights under its separate security over the assets of the franchisees, but merely to assure Extreme that BMO would not enforce the inventory buy-back obligations of ABOT against Extreme.

16 In support of its position, BMO relies on the rule 39.03 examination of a former Denninghouse Group executive, William Thomas. On his examination, Mr. Thomas gave evidence about the history of the relationship between BMO and the Denninghouse Group, the franchisee financing plan, and the Letter of Comfort and Inventory Buy-Back Agreements and

Subordination Agreements between BMO and Denninghouse Inc. Mr. Thomas also gave evidence about the intention of the parties to those agreements, to the effect that it was intended all along that the ABOT GSAs would be subordinated to the BMO GSAs. Counsel for Extreme objects to the admissibility of this evidence, arguing that it amounts to extrinsic evidence of intention, while the agreements themselves were unambiguous. By reason of the conclusion that I have reached as set out below, I find it unnecessary to deal with this argument. I also find it unnecessary to deal with the Extreme argument concerning the scope and intent of the December 10, 2004 BMO comfort letter.

17 In my view, this dispute is governed by the plain language of the Approval and Vesting Order relating to the terms upon which Extreme acquired the assets that it purchased. I have earlier quoted the operative provision of that order. In my view, that language makes it plain that the assets that Extreme acquired were not subject to any higher rights. In this respect, the language of the order is unambiguous and far-reaching. Accordingly, assuming that there had existed an enforceable subordination agreement as between ABOT and BMO in relation to the ABOT GSAs, and assuming that BMO's rights ranked ahead of ABOT's rights, that higher BMO security interest was a right or encumbrance that was deleted by the Approval and Vesting Order.

18 As I have noted above, BMO argues that the Approval and Vesting Order was never intended to have such an effect. As I have also noted, however, BMO was a party to the proceedings, was represented in court when the Approval and Vesting Order was granted, and even provided a comfort letter in order to fulfill one of the conditions for the closing of the sale transaction. I also note that BMO was one of the parties that benefited from the completion of that transaction, as the principal secured creditor of the Denninghouse Group. BMO had ample opportunity to raise the issues of its claimed priority over the ABOT GSAs, and it could have sought to have a suitable limiting provision inserted in the Approval and Vesting Order. It failed to do so.

19 For its part, Extreme was a third party purchaser that was a stranger to the dealings between BMO and the Denninghouse Group. Counsel for BMO points out that Extreme has not taken the position that it was a *bona fide* purchaser for value without notice, and that Extreme had the opportunity to uncover the details of the Subordination Agreements between BMO and the Denninghouse Group prior to closing. Counsel for Extreme concedes that it may well be that the Subordination Agreements between Denninghouse Inc. and BMO were part of the documentation contained in the material made available to prospective purchasers of the assets of the Denninghouse Group. He notes, however, that there is no evidence that Extreme was actually aware of the alleged Subordination Agreements between ABOT and BMO. In any event, he argues, Extreme was entitled to rely on the unequivocal terms of the court order approving the transaction.

20 In my view, it is neither appropriate nor desirable to, in effect, open up and revisit the terms of a vesting order, especially one given two and a half years ago, and upon which parties have subsequently acted and conducted their affairs. It is impossible to say what would have occurred as the parties were negotiating the sale agreement, had the issue of BMO's claimed priority been raised at the time. I am not prepared to speculate that it would have been a matter of no moment: Extreme negotiated for and acquired the assets on the terms set out in the sale agreement and the Approval and Vesting Order. The assets were to be acquired free and clear. BMO was aware of this. BMO failed to protect its claimed position.

21 To paraphrase Cumming J. in *Air Canada Pilots Assn. v. Air Canada Ace Aviation Holdings Inc.* (2007), 26 B.L.R. (4th) 124, [2007] O.J. No. 89 (Ont. S.C.J.) at para. 43, BMO is bound by the Approval and Vesting Order and cannot seek to vary or amend it. As Cumming J. went on to observe (at para. 44):

> The matters resolved by the CCAA Plan and Sanction Order are *res judicata* through issue and/or cause of action estoppel. The doctrine of *res judicata* prevents relitigation of matters which have already been determined by a court of competent jurisdiction.

In the present case, the Approval and Vesting Order was a final judicial determination of the rights of the parties represented in that proceeding in respect of the assets that were the subject of the sale. The CCAA objective of providing a mechanism for the efficient restructuring of corporations that encounter financial difficulty would be seriously undermined if parties who failed to assert or protect their rights at the time of the restructuring were permitted subsequently to return to court to undo past transactions. Such an approach should be discouraged.

22 I therefore conclude that, in relation to the seven ABOT GSAs that are the subject of this application, Extreme has priority over the BMO GSAs.

23 In relation to costs, counsel have agreed that the successful party should be awarded $31,250. I therefore order BMO to pay that amount to Extreme.

Motion granted.