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JEFFREY CARHART & JAY HOFFMAN, Canada's Asset Backed Commercial Paper Restructuring: 2007–2009/ 35

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Canada's Asset Backed Commercial Paper Restructuring: 2007–2009

Jeffrey Carhart & Jay Hoffman[*]

1. INTRODUCTION

Canada's market for non-bank sponsored asset backed commercial paper ("ABCP") froze on August 13, 2007. We became involved immediately after that date, when we were contacted by a number of large ABCP investors.

At that time, we made the decision that we would act for ABCP holders. We did so for a group of mostly corporate ABCP holders, which eventually grew to represent approximately $2 billion worth of ABCP. This group was formally recognized by the Ontario Superior Court of Justice in its administration of the reorganization of the ABCP market proposed by the Pan-Canadian Investors Committee for third-party structured ABCP — which came to be known as the Crawford Committee — pursuant to the *Companies' Creditors Arrangement Act* (the "*CCAA*").[1] We participated actively in the entire process, including the *CCAA* proceedings. We advocated a unique position with respect to the controversial release provisions of the *CCAA* Plan which was adopted by the Ontario Superior Court of Justice. That decision was upheld by the Ontario Court of Appeal and leave to appeal was denied by the Supreme Court of Canada. While space limits alone mean that this article cannot do justice to all of the issues we encountered, it contains a brief discussion of some of the main issues we addressed in the course of this fast moving and historic proceeding.[2]

(a) Canada's ABCP Market

For many years in Canada, the term "commercial paper" referred to a fairly straightforward type of product. Originally, major Canadian companies started sell-

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* Both of Miller Thomson LLP (Toronto). As discussed in this article, the authors represented the Court Appointed Ad Hoc Committee of Asset Backed Commercial Paper Holders throughout the restructuring.

1 *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended [*CCCA*].

2 It has been described as "the largest and most complex restructuring in Canadian history." Jeffrey Leon & Geoffrey White, "The Ontario Court of Appeal's Decision on the Flexibility of the *Companies' Creditors Arrangement Act* in the Restructuring of the Canadian Asset-Backed Commercial Paper Market" (2008) 25(4) Nat'l Insolv. Rev. 45. Similarly, *American Lawyer Magazine* described the ABCP restructuring as "the largest and by far the most complex . . . in Canada's history . . . the only privately negotiated workout of an entire market anywhere in the world." See, Julie Triedman, "Canadian Peacemaker," *American Lawyer Magazine* (August 2008).

ing short term unsecured debt obligations known as commercial paper.[3] In such transactions — involving what has been described as "plain vanilla commercial paper sold (directly) by creditworthy companies"[4] — it could be said the purchaser knew exactly what he or she was buying.

In the 1980's, Canadian banks began sponsoring asset backed commercial paper, which was more complex in nature. Eventually non-bank sponsored ABCP also appeared in the Canadian market and, by August of 2007, Canada's non-bank sponsored ABCP market was worth about $32 billion[5] and was made up of mostly short term debt obligations issued by limited purpose Trusts — also referred to as "Conduits" — that were established by various private sector companies, known as Sponsors. Metcalfe & Mansfield Capital Corp., Newshore Financial Inc. Coventree Inc. and Nereus Financial Inc. were among those Sponsors.

Some of the Trusts issued different "series" of ABCP (or "notes") with different priority ranking and other differentiating features. In turn, the Trusts purchased assets that backed up the ABCP and generated cash flow.[6] Historically, those underlying assets were principally made up of mortgages and various types of consumer loans and receivables; however, by 2007, many of the Trusts had come to hold a significant portion of their assets in the form of more exotic assets such as credit default swaps, collateralized debt obligations ("CDO's") and other leveraged derivatives instruments. In the circumstances, among other things, there was a distinct gap between the relatively short term maturity of any particular ABCP (typically measured in days[7]) and the longer term maturity of the assets held by the Trust in question to back that same ABCP.

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3 See Ontario Securities Commission, *Report of the Task-Force on Debt-Like Derivatives* (Toronto: Ontario Securities Commission, 1999).

4 Janet McFarland *et al.*, "Playing The Blame Game" *The Globe & Mail* (11 August 2007).

5 Of a total asset backed commercial paper market (*i.e.*, including bank sponsored asset backed commercial paper) of about $120 billion. Again, in this article, the term ABCP is used to refer to non-bank sponsored asset backed commercial paper. It may be noted that not all of the ABCP Trusts were ultimately part of the *CCAA* reorganization discussed in this article; for example the Skeena Trust was reorganized independently and the Devonshire Trust was intentionally left out of the *CCAA* proceeding.

6 Trusts were used to hold the assets in order to avoid Canadian taxes, which would have applied if the assets had been held by corporations. Under the terms of the constating Trust documents, the obligations of the trustees (many of whom were trust companies) were limited in recourse to the assets backing the relevant ABCP notes of that Trust. In practice, the trustees delegated the day to day management of the Trust to subsidiaries of the Sponsors. See also, the affidavit of Purdy Crawford, sworn March 17, 2008 in connection with the *CCAA* proceedings.

7 In his affidavit sworn on March 17, 2008, Purdy Crawford noted that "most . . . ABCP is short term commercial paper (usually 30–90 days) . . . the balance of ABCP . . . is extendible for up to 364 days [and some constitutes] longer-term floating rate notes." Indeed, some ABCP was for terms of well under 30 days. In what was obviously a painful situation, some parties bought ABCP for a term of just a few days immediately before the market froze on August 13, 2007.

The market functioned by the repayment of maturing ABCP (which was not "rolled over" into new ABCP) from cash generated by an issuer Trust's underlying asset portfolio and the issuance of new ABCP. As discussed below, the Trusts also paid for liquidity support agreements, which were supposed to provide a source of funding if the Trust was not able to issue a sufficient amount of new ABCP — that is, among other things, the liquidity support agreements were supposed to address the gap between the maturity of the ABCP and the relevant Trust's underlying assets.

(b) Distribution of ABCP

Generally speaking, by 2007, ABCP could be sold to any investor without delivery of a prospectus. In the early 2000's, Ontario securities law[8] had restricted the sale of ABCP, without a prospectus, to individual investors purchasing a minimum of $50,000 worth of paper.[9] Much of the ABCP was also rated by credit rating agencies, such as DBRS, although that rating was not required by securities law at that time. Historically, most Canadian ABCP was rated R-1, the highest rating offered by DBRS.

In 2005, pursuant to National Instrument 45-106, the minimum $50,000 requirement was removed for "commercial paper maturing not more than one year from the date of issue,"[10] if the paper was not "convertible or exchangeable" and as long as it had "an approved credit rating from an approved credit rating organization."[11]

ABCP was sold by many investment dealers. The degree of disclosure provided by the Sponsors with respect to the assets in each Trust was far short of full prospectus-level disclosure. In plain terms, the publicly available informational material with respect to the various ABCP Trusts contemplated that the Trustees could use the funds raised from the sale of ABCP to acquire virtually any type of asset.[12]

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8 Ontario *Securities Act*, R.S.O. 1990, c. S.5, s. 35(2)4 and s. 73(1).

9 Even in the early 2000's the $50,000 stipulation did not apply where the investor was a corporation as opposed to an individual.

10 *Prospectus and Registration Exemptions*, s. 2.35. NI 45-106 (9 September 2005) (Cross reference the "under one year" stipulation, *supra*, n. 7).

11 By 2007, DBRS was the only rating agency rating Canadian ABCP. See Boyd Erman, "Five Things" *The Globe & Mail* (25 August 2007); and Janet McFarland *et al.*, "Playing The Blame Game" *The Globe & Mail* (11 August 2007).

12 For example, the DBRS Report on the Devonshire Trust published August 14, 2006 read in part as follows:

> The Trust can only purchase/loan against Financial Assets funded by an existing Series upon receiving DBRS's confirmation that such purchase/loan would not result in a withdrawal or downgrade of the existing rating of that Series. A ratings test will also apply to a new Series. Apart from this requirement, however, no limitations have been placed on the Trust in terms of potential types of Financial Assets that can be purchased or lent against, provided that the transaction is consistent with the rating of the Notes, Bonds, or FRNs . . . The Trust expects to purchase Financial Assets of various currencies and tenors.

Also, it was very difficult to find any public information about exactly what assets were held by any particular non-bank sponsored ABCP Trust.[13]

(c) The Assets and Liabilities of the Trusts

By 2007, the Trusts had come to hold a variety of assets (of varying degrees of value and complexity) such as the following:

- Some assets were "normal," traditional assets such as non-subprime residential mortgages, commercial mortgages, car loans, equipment loans, credit card receivables and other receivables.
- Some assets were much more complex and less traditional and were classified as "leveraged" and/or "synthetic" and/or "derivatives." For example, some of the Trusts earned periodic cash payments from a counterparty in exchange for providing "insurance" payable to the counterparty upon the occurrence of a designated default on an index of third party debt. In order to secure the Trust's potential obligations under those "credit default swap" arrangements, the Trust in question had pledged some of its assets as collateral in favour of the counterparty. Those pledged collateral assets may have been divided, in turn, as between, for example, cash or "near cash" and various notes. Generally speaking, the Trusts sold "protection" on amounts that were far in excess of the amount of collateral which the Trust had acquired and posted as collateral for its (potential) obligations. However, among other things, the terms of these leveraged, synthetic arrangements typically gave the counterparty the right to make a "margin call" for more collateral in the event of certain specified changes — such as: (i) changes in general credit market conditions; (ii) changes (referred to as "mark-to-market triggers") in mark-to market accounting conditions (which sometimes required a subjective determination by the counterparty); and (iii) changes (referred to as "spread loss triggers") which were tied to levels of certain public indices.
- Some assets were directly tied to the U.S. subprime mortgage market.

In turn, as noted, there were various different "rankings" or series of ABCP of different Trusts in relation to the different portfolios of assets held by the various Trusts. The "riskier" or more subordinate tranches of ABCP Notes gave relatively greater returns as long as the ABCP market functioned. These tranches of ABCP bore such names as Super Senior, Leveraged Super Senior, Junior Super Senior,

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Also, the DBRS Report on the Gemini Trust published June 30, 2006 read, in part, as follows:

> No limitations have been placed on the Trust in terms of potential types of Assets, provided that the transaction is consistent with the rating of the Notes and DBRS has confirmed that such purchase would not result in a . . . downgrade of the existing Notes.

13 For more information, see *infra*, n. 16.

Senior Mezzanine and Junior Mezzanine. In essence, buyers of certain types of ABCP were accessing leveraged exposure to a portion of a pool of assets.[14]

(d) The Freeze of the ABCP Market in August, 2007

As is now well known, the term "subprime" entered general parlance in early 2007.[15] Concern about the extent to which Canadian ABCP trusts held assets linked to the U.S. subprime mortgage market increased. However, as noted above, there was a distinct "lack of transparency" about what assets were held by the various ABCP Trusts[16] and during the summer of 2007 there was considerable angst and uncertainty in the financial community about whether or not any particular ABCP Trust held any subprime assets. In late July of 2007, Coventree circulated a memo to a select list of industry recipients concerning the amount of subprime exposure of any particular ABCP Trust that they had sponsored;[17] however, generally speaking, answers to the spreading questions about what assets were held by the ABCP Trusts were in limited supply.

Eventually, the freeze occurred on August 13, 2007, when a number of sponsors of non-bank managed ABCP announced that they were unable to place new ABCP. A crisis of confidence had hit and there were simply no buyers. In turn, as discussed in more detail below, the liquidity support agreements that these Trusts had paid for proved to be of no assistance in the circumstances. Most of the liquidity providers denied funding on the basis that they had only agreed to provide such funding in the event of a *general* market disruption — *i.e.*, one more broadly based than the disruption which seemed so very real and had undeniably occurred in August of 2007.[18]

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14 Claude Bergeron, "The Worldwide Commercial Paper Crisis: A Canadian Perspective" *Caisse de dépôt et placement du Québec* (September, 2008) [Bergeron].

15 2007 represented the end of a period of remarkable credit availability. The emergence of the U.S. subprime mortgage industry (which has been called "evil incarnate" by Donald Drummond, Chief Economist of TD Bank) and the attendant collateralization and syndication of those mortgages represented some of the results of those conditions. As harbingers of what was to come, in early 2007, some Bear Stearns and BNP Paribas funds either filed for bankruptcy protection or were frozen amid concerns about their exposure to the subprime market. Bergeron, *ibid.*

16 In his Affidavit sworn on March 17, 2008, Purdy Crawford commented:

> Investors who bought ABCP often did not know the particular assets or mix of assets that backed their ABCP. In part, this was because ABCP was often issued and sold before or at about the same time the assets were acquired. In addition, many of the assets are extremely complex and parties to some underlying contracts took the position that the terms were confidential.

17 Thomas Watson, "Credit Markets: Issues of Trust" *Canadian Business Magazine* (5 November 2007).

18 The Canadian Banks continued to sell or "roll" their sponsored asset backed commercial paper after August, 2007 — presumably due to the relative strength of the liquidity support behind that bank sponsored paper. The pricing on the bank sponsored paper after August, 2007 reflected more adverse market conditions.

(e) Canadian Style Liquidity Agreements

During the Cuban Missile Crisis, Robert Kennedy remarked that in an emergency Canada will give you all aid short of help.[19] That comment came to mind when we looked at the liquidity agreements which pertained to these ABCP Trusts.

In Canada, the typical liquidity support agreement — known (one must acknowledge, not in a positive way) as a "Canadian Style Liquidity Agreement" — provided that support would only be made available in the event of a "general market disruption." In essence, this language meant that the support would only be made available when the *entire* Canadian asset backed commercial paper market — and not only the non-bank sponsored subset of that market — had collapsed. The Canadian Style Liquidity Agreements were in contrast to Global Style Liquidity Agreements, which were structured to provide support if the cash flow to investors were impaired "for virtually any reason."[20] We understand that Global Style Liquidity Agreements were used for bank sponsored asset backed commercial paper in Canada, as opposed to the *non*-bank sponsored paper that is defined as ABCP in this article.

In 2004, the Office of the Superintendent of Financial Institutions ("OSFI") amended its existing Guideline B-5 to provide that banks under its supervision did not have to allocate capital towards potential obligations under these Canadian Style Liquidity Agreements.[21] In other words, OSFI clearly seemed to recognize the unlikelihood of a bank ever having to fund anything under these Canadian Style Liquidity agreements — hence no capital needed to be set aside, in OSFI's view, in connection with the Banks entering into such agreements. OSFI has stated that, through this period, "it made clear that it was not dictating what type of lines should be used for Conduits; that was a decision for the Conduit creators and investors, and rating agencies to make." "OSFI's role," OSFI has gone on to say, "was limited to insuring that . . . whatever types of loan commitment banks entered into, appropriate capital would be charged . . . [and] the roles and responsibilities of Canadian banks were clear."[22]

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19 Robert F. Kennedy, cited in Michael Adams, "Continental Divide" *The Walrus* 1:4 (April/May 2004) 62 at 63; and in Allan Fotheringham, *Capitol Offences* (Toronto: Key Porter Books Ltd., 1986) at 1.

20 OSFI, Press Release Backgrounder, "OSFI's Role in the ABCP Market Issue" (22 April 2008) at 3. In 2002, Standard and Poors described the Canadian Style "condition for a liquidity line advance [as] narrow to the point of being almost meaningless." See Sean Silcoff, "The House that Alan Built" *National Post* (18 August 2007). As discussed in note 11, Standard & Poors and all ratings agencies other than DBRS had stopped rating Canadian ABCP by 2007. In that regard, it may be noted that the April 2008 OSFI Press Release stated that "the fact that Canadian investors were buying ABCP with one rating and limited liquidity was . . . known. S&P had put out reports explaining why they would not rate a product that had liquidity lines that could only be drawn in the event of a general market disruption."

21 OFSI, *OSFI Guideline No. B-5: Asset Securitization* (Ottawa: Office of the Superintendent of Financial Institutions Canada, 2004).

22 OSFI, Press Release Backgrounder, "OFSI's Role in the ABCP Market Issue" (22 April 2008) at 4.

In mid January, 2007, DBRS adjusted its methodology with respect to ABCP to reflect a recognition that the liquidity lines then held by most Canadian ABCP Trusts would not prove to be of assistance in the event of a disruption in the non-bank sponsored ABCP market.[23] DBRS has noted that purchasers of asset backed commercial paper seemingly paid no premium for notes supported by Global Style Liquidity Agreements.[24] In other words, as one can imagine, the Canadian Style Liquidity Agreements were cheaper for the Trusts to purchase than Global Style Liquidity Agreements. In theory, this difference should have been reflected in the yields or pricing of non-bank sponsored ABCP which had such "cheaper" liquidity support; however, in practice, by the summer of 2007, that was not the case.[25] Rather, in the summer of 2007, ABCP was priced as if it had less risk associated with it than was actually the case.

(f) The Montreal Accord

When the ABCP market froze, among other things, certain financial institutions (known as the "Asset Providers") that contracted to receive protection from the Trusts against defined credit events, notified certain Trusts that the Trusts were required to post additional collateral to support their obligations owed to the Asset Providers under the credit default swap arrangements, failing which those Asset Providers could seize the collateral which had been pledged to them. Some of those financial institutions were the same institutions who had agreed to provide (Canadian Style) liquidity support agreements to the Trusts also in exchange for fees. Simply put, if that process had been allowed to unfold, the value associated with the Trusts could have collapsed entirely; the "secured parties" would have taken the pledged collateral, potentially leaving little or nothing for the ABCP Noteholders.

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23 Dominion Bond Rating Service, Press Release, "DBRS Revises CDO Criteria for Canadian ABCP Issuers" (19 January 2007).

24 Matthew McClern, "Inside a Crisis" *Canadian Business Magazine* (5 November 2007) 128 at 133. In September, 2007, DBRS indicated that it would thereafter require all new Canadian issuers of ABCP to hold Global Style Liquidity Agreements.

25 As relatively cheap as these Canadian Style Liquidity Agreements might have been, one had to ask the question of what value had ever been received by a Trust in exchange for the payment for these agreements? Of course the agreements proved to be of absolutely no value right up to the point where the Trusts were staring into the abyss. Accordingly, was it merely a question of unjust enrichment for the "liquidity" providers to have received a fee when, in effect, they provided no assistance to the Trusts? One could pursue this line of thinking to contemplate an argument that in a truly global financial shutdown — of the type where even a Canadian Style Liquidity Agreement would be engaged — the financial institution on the other side of the agreement would be in the middle of a global financial calamity and might be unable to perform for that reason (taking you back to a scenario where, once again, the Canadian Style Liquidity Agreement was never, and could never be, useful). There is serious doubt as to whether any individual ABCP Noteholder really had the legal right to bring an action against the liquidity providers or in connection with the liquidity support agreements. The widely held view is that it was up to the Trustees to pursue those kinds of claims and actions. See the discussion under section 1(h) of this article.

On August 16, 2007, a group of financial institutions (including investors in, and distributors of, ABCP; institutions that had provided liquidity facilities to the Trusts; Asset Providers and shareholders of certain Sponsors) agreed to what then came to be known as the Montreal Accord. Under that arrangement these institutions — and other holders who later signed on — agreed to a standstill period.[26] During this standstill period, each party agreed that, among other things, it would roll over its ABCP on or following its maturity date and would not take any action that would precipitate an event of default under the relevant Trust indenture governing the ABCP.[27] This agreement included a pledge by Asset Providers to refrain from making any collateral calls on assets held by the Trust and a pledge by Trust Sponsors to refrain from pursuing efforts to recover from any liquidity provider who signed on to the proposal.

Additionally, the participants in the Montreal Accord agreed to a proposal that would see ABCP eventually converted to floating rate notes with maturities that would match the maturities of the underlying assets. At that early stage, it was stated that this proposal would ultimately be subject to the approval of the requisite number of holders of ABCP in each Trust.

Ernst & Young was retained by the signatories to the Montreal Accord to assist in the collection and dissemination of information of interest to holders of ABCP.

(g) The Crawford Committee

On September 6, 2007, an investors committee chaired by Purdy Crawford was formed to oversee the proposed restructuring process resulting from the Montreal Accord. That committee — officially known as the Pan-Canadian Investors Committee for Third-Party Structured Asset Backed Commercial Paper and, as noted, more commonly known as the Crawford Committee — included particular investors who were signatories to the Montreal Accord, plus certain other parties.

On November 22, 2007 Purdy Crawford wrote an article[28] outlining aspects of what the Crawford Committee intended to achieve. In that article, Mr. Crawford indicated that the plan was designed to prevent "the default of most . . . ABCP and the accompanying destruction of value that a "fire-sale" liquidation would undoubtedly have caused." Mr. Crawford also indicated the Committee was working with JPMorgan to analyze the assets, underlying structures and relevant legal documentation of the Conduits, with a view to creating "transparency as soon as we can." However, he also noted the continued importance of confidentiality of market sensitive information regarding the underlying assets. Further, Mr. Crawford indicated an intention to present a plan in December, 2007.

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26 The original standstill period was 60 days. It was subsequently extended a number of times.

27 There was significant consternation in the early days of the ABCP freeze over the issue of whether it was necessary, under the terms of the Trust indentures, for ABCP holders to go through the motions of trying to roll over the ABCP — even unsuccessfully — in order to maintain a claim to the continuing accrual of interest on the principal amount of the ABCP. Some of the Trust indentures seemed to require that process.

28 Published that day in the *National Post*, page FP3.

(h) Extraordinary Resolutions

Through the fall of 2007, our clients were faced with requests to sign various extraordinary Trust resolutions, including standstill resolutions. Under the terms of the various Trusts, resolutions were circulated during that period to provide for such matters as:

- the Trusts becoming party to the Montreal Accord; and
- the Trusts not pursuing litigation or other activity with respect to the liquidity support facilities.[29]

These resolutions went on to provide that the Trustee in question was both absolved of any claims with respect to prior activities and instructed not to undertake investigations with respect to the options available to protect the Noteholders. Many ABCP holders refused to sign these extraordinary resolutions.

(i) Accounting Provisions

In the fall of 2007, the ABCP Noteholders were also faced with the task of trying to account for their losses on the frozen ABCP for accounting purposes. This challenge was really an art as opposed to a science as companies were required to estimate the market price of their ABCP at a time when the market had been frozen since August, 2007 and also explain how that estimate was determined. Among other things, we did our very best to gather information about what various parties announced, as a matter of public record, with respect to write downs of ABCP.

(j) Maintenance of Standstill Arrangements

The Crawford Committee was generally successful in maintaining the overall standstill arrangements contemplated by the Montreal Accord. In early November, 2007, Perimeter Financial Corporation announced plans to begin listing "as many as 30 different issues of ABCP on its . . . trading system."[30] However, the Perimeter trading facility did not attract any significant activity.

2. ESTABLISHMENT OF THE AD HOC COMMITTEE

Our thinking, from an early date, was that it was desirable to have the Crawford Committee recognize both our ad hoc Committee of ABCP holders and a funded independent financial advisor for our Committee. We felt it would be difficult for even sophisticated clients to assess and respond to the detailed terms of the proposed restructuring, which we knew would be forthcoming without independent professional advice.

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29 This "passive" stance was put forward as being in keeping with the standstill aspects of the Montreal Accord. It should be noted that some of the financial institutions who had provided the liquidity support agreements were also the parties being asked to contribute financially to the proposed new (enhanced) structure of the restructured paper.

30 Jacquie McNish & Boyd Erman, "Upstart to trade frozen debt" *The Globe & Mail* (2 November 2007).

(a) Confidentiality Arrangements

In that regard, it was clear early on that our clients would have very limited access to meaningful information about the assets of each Conduit prior to the release of an information statement with respect to the reorganization, unless they agreed to detailed confidentiality arrangements.

In turn, the Crawford Committee took the position that, among other things, our clients would not be able to use any information they received through the disclosure process for any purpose other than considering the restructuring proposal they could expect to be forthcoming. In particular, therefore, our clients could not use such information in the course of litigation.

In that regard, the provisions of the confidentiality agreements we ultimately signed made clear that certain lawyers in our firm who were going to be able to gain access to the information could not thereafter participate in certain types of litigation pertaining to ABCP under any conditions (i.e., including if the reorganization was unsuccessful for any reason).

While the use of confidential information was restricted, the confidentiality agreements did not prohibit the commencement of litigation if the reorganization ultimately did not proceed; as such, it seemed possible that any Noteholder who did ultimately form the decision to proceed with a lawsuit at such a stage would be entitled to secure access to the necessary documents through discovery and the balance of the litigation process.

On balance, these arrangements were acceptable to our clients who accepted the basic legitimacy of confidentiality requirements. In particular, we respected the fact if the information about the assets in the Trusts got into the wrong hands (before the restructuring could be completed or be given the chance to be completed) it could be misused to the detriment of *all* ABCP holders. Eventually we negotiated and signed the terms of detailed confidentiality agreements that permitted access to certain confidential information concerning the Trusts, the ABCP relating to the Trusts, the ABCP and the proposed restructuring.[31]

(b) Financial Advisor

As noted, we indicated to Mr. Crawford that we thought that it was vital for the Crawford Committee to recognize the appointment of a single qualified independent financial advisor, in order to address the issues resulting from the lack of available information about the assets in each Trust. We noted that the restructuring proposal that would ultimately be forthcoming would understandably be detailed

31 Of course, what even this important information could not be expected to speak to was all of the detailed facts which "went behind" any individual purchase of ABCP from a particular dealer institution. ABCP holders were being asked to give releases with respect to those circumstances without the benefit of a litigation process — or any other claims process — to know with precision as to the full extent to which they could make out a claim (whether based on fraud, negligence, wilful misconduct, a failure of a securities dealer to know his or her client or on some other basis). Certainly, many ABCP holders felt that such a claim existed.

and complex on a Trust by Trust basis.[32] In our view, such an advisor, with appropriate legal support, could build up a familiarity with the methodologies used by the Crawford Committee — and its advisor JPMorgan — and their approaches with respect to the complex reorganization of the Trust assets. Being able to work with such advisors, we felt, would also allow our clients to reach their decision as to how they were going to vote with respect to the reorganization in a much quicker manner than would otherwise be the case. We put forward PricewaterhouseCoopers Inc. as financial advisor to the Ad Hoc Committee.

(c) The Release Issue

Early on in the process we recognized that one of the cornerstones of the reorganization was going to be that all holders of ABCP would be called upon to release any claims they had in connection with their original acquisition of the ABCP. In turn, we advised our clients that that type of result could only be achieved through the *CCAA*.

In 2006 and early 2007, we were involved in a major *CCAA* case known as *Muscletech*, which involved the international reorganization of an insolvent group of companies that had sold products containing the drug ephedra.[33] In that *CCAA* case, a number of "third parties" — such as retail stores which sold the drug products, and insurance companies — participated in the reorganization. In turn, at the end of the process, those third parties, as well as the Muscletech group of companies, received the benefit of comprehensive releases. As discussed in *Reflections on the Muscletech Case*, we felt that such releases had been justifiable on the factual basis of that case. This issue is discussed in more detail below, but it may be noted at this point that, in the fall of 2007, we alerted our clients to the fact that it was likely that, in due course, the reorganizational proposal being pursued by the Crawford Committee could only be accomplished pursuant to the provisions of the *CCAA*. As is also discussed in *Reflections on the Muscletech Case*, we felt that one

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32 Realistically, we also understood from an early stage that only a broad based "global" restructuring of many of the frozen Trusts under one *CCAA* proceeding would make sense. Theoretically, it would have been possible to have pursued numerous individual *CCAA* plans — one for each Trust. However, each such *CCAA* plan would have been conditional on all of the other such *CCAA* plans being implemented. Accordingly it seemed to us that it made more sense to consolidate the *CCAA* proceedings; however, again, it was therefore also clear that the resulting "global" package would be enormously complex (earning, we predicted, the kinds of descriptions recorded in note 2).

33 See Jeffrey C. Carhart, "Reflections on the Muscletech Case" in Janis P. Sarra, ed., *Annual Review of Insolvency Law 2007* (Toronto: Thomson Canada, 2008). The *Muscletech* case generated numerous reported decisions, which are cited in that article. The main company in that case was called Muscletech Research and Development Inc. At one time, the sale of ephedra was extremely remunerative. However, eventually the drug was declared to be illegal in both Canada and the U.S., in the wake of many lawsuits against the companies that had been marketing ephedra products alleging various adverse effects from the use of the products (including both injuries and deaths). The Muscletech group of companies initiated a *CCAA* proceeding and an ancillary proceeding under Chapter 15 of the U.S. *Bankruptcy Code* with the goal of resolving the various litigation against it.

of the fundamental "lessons" of the case was that anyone objecting to the concept of third party releases in a *CCAA* plan should make their concerns known at the earliest possible appropriate point in the *CCAA* proceeding.

3. THE FRAMEWORK AGREEMENT

On November 26, 2007, the Crawford Committee announced that they had agreed on the basis of a restructuring plan. On December 23, 2007, a formal Framework Agreement was announced.

The new structure involved the creation of three master asset vehicles or "MAVs." For the old series of ABCP notes that had been comprised exclusively of traditional assets, those assets would be transferred to MAV3 and the holder of the old notes would receive tracking notes issued by MAV3 based on the pool of assets in that particular exclusively traditional series. The new notes would be termed out so the maturity date would approximate the maturity of the assets in the relevant new Conduit.

Holders of notes in old ABCP series that included ineligible assets, which were underperforming assets comprised primarily of U.S. subprime mortgages, would receive separate tracking notes that would also be segregated and would track the performance of the underlying ineligible asset. There would be a separate tracking note issued for each ineligible asset. Again, the term of the note would match the term of the underlying ineligible asset.

Any series of old ABCP notes that included a mix of synthetic and traditional assets would be pooled in either MAV1 or MAV2. This pooling would result in the assets of 30 different series of old ABCP notes being included in these new MAVs. The pooling of assets would allow the Asset Providers to cross-collateralize trades, improving the position of the Asset Providers in the event of a margin call on a particular synthetic instrument. Pooling would also make it easier to negotiate with the Asset Providers, as it would be less time consuming and more economic to negotiate one solution for all the synthetic trades rather than negotiating on a series-by-series basis for 30 series of notes.

The Asset Providers agreed to change the old mark-to-market triggers to more objectively determinable spread loss triggers and, most importantly, to restructure the trigger levels so that they would be more remote than the triggers currently in place. In addition, to the extent that the new, more remote triggers would be breached, there would be a commitment for margin funding to meet future margin calls if necessary. This new credit facility would be in the amount of $14 billion. This credit facility would be made available by a combination of investors, Asset Providers, dealer Banks and other financial institutions.[34]

Under the proposed restructuring, the difference between MAV1 and MAV2 was that, in MAV2, the margin funding would be provided by Canadian Chartered Banks and foreign bank Asset Providers, whereas, in MAV1, the Noteholders would be self-insuring. The total amount of margin funding facilities would be

34 The Crawford Committee continued to negotiate the terms of the margin funding facility until March, 2008.

about $13.5 billion. The leveraged synthetic instruments in these pools would also be supported by $8.5 billion of new collateral.

Each of MAV1 and MAV2 would issue four classes of notes. The Class A-1 and A-2 Notes would be senior notes that were expected, at that time, to be rated AA by DBRS and another rating agency. The Class B and Class C Notes would be subordinated notes that were not expected to be rated. Each holder would receive notes in each Class aggregating the face amount of the relevant series of their existing ABCP. The amount of the Class A-1 Notes would represent the entire "indicative value" of the old notes to be exchanged for the new notes of MAV1 or MAV2.

Again, of course, the proposed restructuring was tremendously complex and massive in scope. It involved not one, but 20 separate debtors and numerous market participants and, perhaps, most noteworthy, it was to take place against the backdrop of an unprecedented widening and contracting of credit spreads before and after the framework of the restructuring had been agreed to by the parties involved.

Clearly, the deteriorating credit markets had an adverse impact on the value of the notes issued by the Trusts and created a tremendous amount of uncertainty, all of which made the case for acceptance of the restructuring proposal more compelling to many ABCP Noteholders. At the same time, the credit market conditions appeared to strengthen the position of the Asset Providers as, by March of 2008, most of the credit default swaps triggers were either breached or were within 10% of being breached. This would have allowed the Asset Providers to demand more collateral and ultimately to unwind the trades, which could have had a domino effect given the unprecedented number of trades that would be affected.

Of course, the widening spreads also made it much more challenging to find lenders willing to provide the margin funding facility at an acceptable cost. In addition, the market conditions made it difficult to obtain the desired ratings on the new notes and it prevented those notes from being rated by a second rating agency.[35] We also understood that the market conditions contributed to the inability of the Crawford Committee to find a liquidity solution for holders of new notes that could not hold to maturity for economic or regulatory reasons.

4. CHALLENGES FACING HOLDERS OF ABCP

In the circumstances, the proposed restructuring presented a difficult set of challenges for ABCP holders, including the following:

- There was the basic fact that short-term notes had been frozen since August 2007. As discussed, some Noteholders purchased ABCP for a period of just a few days, commencing on August 10, 2007. Others invested a substantial portion of the proceeds of public offerings earmarked for large projects. Clearly the lack of liquidity had put a severe strain on many holders of ABCP.
- The total lack of transparency of the old Trusts and the inability to access meaningful information on the assets underlying the notes until the mid-

35 Only DBRS would rate the new paper.

dle of March, 2008 — and even then some critical information concerning the new notes remained unavailable — made it very difficult for Noteholders to assess their situation.

- Many corporate Noteholders experienced uncertainty and difficulty around valuing their existing notes for financial reporting purposes.
- Many Noteholders had struggled with the complexity around the new structure and the change from a short-term investment to a long-term note with no assurances of a liquid secondary market.
- Questions were raised around the fairness of the treatment of different series of existing notes under the restructuring. For example, there were questions about what, if any, benefits accrued to Noteholders who received MAV3 tracking notes backed by traditional or ineligible assets. There were also questions around the fairness of pooling to holders of certain series of notes comprised of exclusively unleveraged synthetic asset pools who, instead of receiving MAV3 tracking notes in respect of those asset pools, were to be exposed to significant additional risk by being pooled with leveraged synthetic assets in MAV1 and MAV2.
- Noteholders struggled to value the proposed new notes.
- The process to approve the restructuring and the related comprehensive releases required difficult decisions to be made by holders of ABCP who believed they had good claims against certain market participants. With respect to this last point, however, in the final analysis, and as the calendar moved from 2007 to 2008, our position was that the time had come for our clients to focus their efforts on working with Crawford Committee process as long and as far as possible. There would not be a second chance to do that.[36]

5. THE CCAA PROCEEDING

The initial *CCAA* filing was made with the Ontario Superior Court on March 17, 2008 on the application of the members of the Crawford Committee (sometimes thereafter referred to as the "Applicants" in the *CCAA* proceeding).

One of the interesting aspects of the *CCAA* filing was that, as its full name implies, the *CCAA* is designed to apply to *companies*, not trusts. In that regard, however, companies had been installed as trustees of one or more of the ABCP Trusts (or Conduits) with effect immediately prior to the *CCAA* application. Those companies — known as the "Respondents" in the *CCAA* proceeding — assumed legal ownership of the assets of each ABCP Trust and assumed the obligations of the

36 In contrast, of course, there would always be plenty of time for litigation if the *CCAA* process was ultimately not successful. We spent significant time working with the Crawford Committee and JPMorgan in February and early March, 2008, after, among other things, negotiating and signing the confidentiality agreements referred to in section 2(a) of this article.

Trustees who they had just replaced (each of whom would not have qualified as a "debtor company" within the requirements of the *CCAA*).[37]

Counsel for the Crawford Committee represented the Applicants. At the time of the *CCAA* filing, a detailed *CCAA* Plan of Compromise and Arrangement and an Information Statement, all based on the terms of the Framework Agreement, was submitted to the Court. The bound Plan materials resembled a telephone book for a major city and, among many other things, contemplated unlimited releases for a host of parties associated with the distribution and sale of ABCP and the efforts of the Crawford Committee. The proposed beneficiaries of the unlimited releases (broadly defined as the "Released Parties") included parties who were making undeniable, significant contributions to the proposed new structure as well as parties whose involvement in the "go forward" structure seemed much more remote, if not non-existent. In plain terms, however, the Accompanying Information Statement acknowledged that, "the Released Parties (including those Released Parties without which no restructuring could occur) require that all Released Parties be included so that one person who is not released by the Noteholders is unable to make a claim-over from a Released Party and thereby defeat the effectiveness of the release."[38]

It may also be noted that while the initiation of the *CCAA* proceeding resulted in a broad court ordered stay of proceedings against the *CCAA* debtors, proceedings were not stayed with respect to the numerous synthetic derivative contracts which

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37 In his decision — reported as *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), [2008] O.J. No. 1818, 2008 CarswellOnt 2652, 45 B.L.R. (4th) 201, 42 C.B.R. (5th) 90 (Ont. S.C.J. [Commercial List]) [*ATB Financial*] — Justice Campbell of the Ontario Superior Court stated that:

> The problem faced by the [A]pplicants in this proceeding is that the terms "company" and "debtor company" as defined in s. 2 of the *CCAA* do not include trust entities.
>
> For the purpose of this Application and proposed Plan, those entities that did not qualify as "companies" for the purposes of the *CCAA* were replaced by Companies (the Respondents) that do meet the definition.
>
> I am satisfied in the circumstances that these steps are an appropriate exercise of legally available rights to satisfy the threshold requirements of the *CCAA*. I am satisfied that the change in trustees was undertaken in good faith to facilitate the making of this application.
>
> The use of what have been called "instant" trust deeds has been judicially accepted as legitimate devices that can satisfy the requirement of s. 3 of the *CCAA* as long as they reflect legitimate transactions that actually occurred and are not shams.

This liberal jurisprudence concerning qualifying trust entities for *CCAA* proceedings is important given the extensive use of trust vehicles — particularly income trusts — in Canada over the last decade.

38 Ernst & Young Inc., "Information Statement concerning Proposed Restructuring of Canadian Third-Party Structured Asset-Backed Commercial Paper" (30 March 2008) at 127, online: <www.ey.com/ca/commercialpaper>. This Information Statement, along with all of the other material from the *CCAA Proceeding* was available on the website of Ernst & Young, which was the Monitor in the *CCAA* proceedings.

constituted an enormous portion of the overall assets of the Trusts. The reason for that fact is the *CCAA* cannot restrain the exercise of rights under "eligible financial contracts"[39] and most of the synthetic derivative contracts in this case constituted eligible financial contracts. Accordingly, as the *CCAA* case moved forward there were always two "stays" at work — the one imposed by the Court pursuant to the *CCAA* and the consensual one agreed to by the Asset Providers. Each regularly had to be renewed, creating a constant level of tension surrounding the process.

(a) The Appointment of Representative Counsel to the Ad Hoc Committee and the Ad Hoc Committee's Financial Advisor

An order was made on March 17, 2008, recognizing both the Ad Hoc Committee and the appointment of Miller Thomson LLP as counsel to that Committee and PricewaterhouseCoopers Inc. as financial advisor to the Ad Hoc Committee. The Applicants, the Canadian Banks and the Asset Providers consented to that appointment order.

(b) The Position of the Ad Hoc Committee on the Initial *CCAA* Filing

At the time of the initial *CCAA* application, we were in a position to confirm to the Court that:

- the Ad Hoc Committee supported the decision of the Crawford Committee to initiate the *CCAA* proceedings as a process to seek a consensus on the terms of the proposed restructuring;
- the Ad Hoc Committee believed that the *CCAA* process would best ensure a successful implementation of the restructuring; and
- therefore the Ad Hoc Committee was of the view that the Crawford Committee should be given the opportunity to advance the terms of the proposed restructuring within the context of the proposed *CCAA* proceeding.

Our March 17th court materials also noted our concern about the release issue at that stage; in that regard, the affidavit in support of our Notice of Motion stated, in part, that:

> The Proposed Restructuring outlined in the Draft *CCAA* Application Record identifies a number of complex legal and financial issues on which the holders of ABCP will require advice. The Draft *CCAA* Application Record requires that such holders provide comprehensive releases as a condition to participation in the Proposed Restructuring and that holders vote to approve the Proposed Restructuring in one class of Noteholders. The Ad Hoc Committee has identified these issues (among others) as ones on which it requires representation to advise it and its constituent members on the terms of the Proposed Restructuring.

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39 *CCAA, supra,* n. 1 at s. 11.1(2).

(c) The Hearing Before the Vote

Our concerns over the release issue came to a head on April 22, 2008, when a hearing took place in advance of the meeting of creditors to vote on the *CCAA* plan.[40]

As noted above, we had advised our clients that one of the lessons of the *Muscletech* case was that it was necessary to alert the *CCAA* debtors and, as appropriate, the Court, of concerns over the release issues as quickly as possible. The problem is that what constitutes "as quickly as possible" seems to keep getting faster and faster.

For example, as discussed in *Reflections on the Muscletech Case*, the *Muscletech* case (which itself moved at a very brisk pace) was built around a claims process. Generally speaking, in that case, it was clear from the point of the initiation of the claims barring process that third party releases would be a central feature of the *Muscletech* plan. As such, it was really incumbent on parties who objected to the very idea of third party releases to do so at the claims stage rather than at the stage of the creditors' meeting or the sanction hearing.

In the ABCP case, things were moving even faster. After an Initial Order in mid-March of 2008, the vote was scheduled for April 25, 2008, and there was not going to be a claims barring process. The Plan simply was what it was.

Accordingly on April 22, 2008, we took the following essential positions before the Ontario Superior Court:

- The releases should not be absolute in nature. In other words, we thought that there should be a carve-out from the releases. Initially we advocated that this carve-out should include fraud, gross negligence and wilful misconduct. Our position was that these were still relatively early days in the ABCP situation and there was a very real concern, on the part of our clients, that facts which were not in the public domain could become known, thereby justifying some form of action. Our clients were almost all corporations and the officers of those corporations dealing with this difficult matter had to explain it to, and seek the approval of, their boards of directors. The direction we had from our clients was that those boards would have a very difficult time approving the plan without carve-outs from the releases.[41]

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40 By this time the Crawford Committee had participated in a series of "town hall" meetings across Canada to explain and discuss the Plan. Many of the attendees at these meetings were so-called "retail investors" — individual people with ABCP holdings of under $1 million. Following that process a deal was struck — and the Plan was amended accordingly — to stipulate that if the Plan was passed, approved by the Court(s) and implemented, those retail investors would be "made whole" through a purchase of their ABCP by certain financial institutions previously involved in the ABCP market.

41 Our view was that the Canadian jurisprudence indicated that some type of carve-out (for fraud, wilful misconduct, etc.) from third party releases had typically been given in *CCAA* cases. *Muscletech* was the only significant case where no carve-out was provided. However — and this was always a critical part of our position — it seemed arguable that in *Muscletech* the creditors received what could be described as "full value"

- As a secondary suggestion, we advocated a change in the creditor classification for voting purposes. In that regard, we made the point that Noteholders who were participants in the ABCP market should only be in a position of being able to "vote to give themselves a release" if the release had been scaled back appropriately. As we said, it is one thing for people to vote to give themselves an appropriate release, but it did not seem acceptable for people to vote to give themselves an unlimited release.

We did not seek an adjournment of the vote, although that relief was requested by some other ABCP holders who took the position that the release should be removed entirely.

In his ruling,[42] Justice Campbell allowed the vote scheduled for April 25, 2008, to proceed on schedule, but stated that "there is a very serious issue of law of the legally permissible extent of third party releases."[43] Accordingly, Justice Campbell held (in paragraph 12 of his decision) that parties were entitled to vote "while preserving their ability to argue both validity and fairness of specific releases."[44]

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for their claim. Of course, saying what constitutes "full value" for a tort claim is an art rather than a science to some extent. Certainly it can be acknowledged that many people have filed tort claims in excess of the amount that they either end up settling for or that they are awarded by a court. However, the point that we made was essentially as follows: any knowledgeable lawyer with expertise in tort claims can assess the value of those claims within a certain range. The range has to be based on a qualified medical assessment of the injuries suffered. In *Muscletech*, the claims process was based around a mediation process whereby such qualified medical analysis would be brought to bear in assessing and valuing the claims. To that extent, again, we felt it was fair to say that in *Muscletech* the people participating in the *CCAA* plan and, in effect, "giving the releases," accepted that they were getting full value for their claim. As we said in court, there is an old political expression that "there is only one tax payer" and in that regard, our position was that "there is only one claim" in the sense that no matter how many people someone might be suing, as soon as that person gets something that *that person* accepts as representing a satisfactory "full value" for their claim from any one or more of the defendants, then logically there is absolutely no reason why that creditor would not then be willing to release all of the parties — because there is nothing left to recover on that "one claim." Regrettably, however, in the ABCP case two facts seemed very clear: (i) there would be no "art versus science" aspect to valuing the claims; instead, it would be painfully clear to each of our clients what dollar value they were entitled to and what the shortfall would be between the value of that entitlement and the value of what would be available to them, at least in the immediate term, under the reorganizational plan; and (ii) therefore, there would be a real ascertainable cost to giving the releases.

42 *ATB Financial*, *supra*, n. 37. Justice Campbell also called for the ABCP holders, including the members of the Ad Hoc Committee, to particularize their claims. Of course, as we and other counsel pointed out, the ABCP holders did not have all of the relevant facts; however, extensive information, including a description of the various causes of action that seemed to be available, was provided to Justice Campbell.

43 *Ibid.*, at para. 13.

44 *Ibid.*, at para. 12.

In the circumstances, the vote proceeded on the 25th of April, 2008. We read a statement into the record at the meeting to the effect that, among other things, those in our committee who were voting "yes" preserved their right to argue fairness and validity of the release provisions in accordance with paragraph 12 of Justice Campbell's decision; in turn, those who were voting "no" did not mean to signify that they were insisting on no compromise of any of their litigation rights, again in accordance with paragraph 12 of Justice Campbell's decision.

(d) The Original Sanction Hearing

Relentlessly, the matter then came back before Justice Campbell in a fulsome two day sanction hearing on May 12 and 13, 2008.

By that time our Ad Hoc Committee's membership had increased from 14 parties holding approximately $1.2 billion in ABCP to 31 parties holding approximately $1.8 billion in ABCP.

At that time we reiterated some of our core concerns with respect to the release issue, including that:

- there had been no formal claims process so as to enable the Court to know exactly what was being released; and
- the members of our Ad Hoc Committee were simply not in possession of enough information about the marketing, sale, funding and sponsorship of the ABCP marketplace to know what they were and were not releasing.

As we also said at that time, in the words of Justice Blair (then of the Ontario Court General Division), "fraud . . . unravels all."[45] It just did not seem open to ask a court to absolve people from responsibility for fraud in these circumstances.

In taking our position, we were well aware of the severe pressures our clients were under.[46] Among other things they needed to choose between the possibility of foregoing the undeniable benefits of the Plan,[47] while fighting to preserve a right to

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45 *885676 Ontario Ltd. (Trustee of) v. Frasmet Holdings Ltd.* (1993), 1993 CarswellOnt 186, [1993] O.J. No. 113, 17 C.B.R. (3d) 64, 12 O.R. (3d) 62, 99 D.L.R. (4th) 1, 30 R.P.R. (2d) 1 (Ont. Gen. Div. [Commercial List]) at paras. 37-38, citing *Angelica-Whitewear Ltd. v. Bank of Nova Scotia*, EYB 1987-67726, 1987 CarswellQue 24, 1987 CarswellQue 91, [1987] S.C.J. No. 5, [1987] 1 S.C.R. 59, 73 N.R. 158, 6 Q.A.C. 1, 36 D.L.R. (4th) 161, 36 B.L.R. 140 (S.C.C.) at 71 and 83 [S.C.R.] [*Frasmet Holdings*].

46 We were also aware of the fact that the eyes of the world were on Canada's legal and financial community and its reputation in this case.

47 By this time we had a deep appreciation of the effort, skill and value that had been brought to bear by Purdy Crawford and his team in designing the Plan. For posterity, the concluding paragraph of the lengthy affidavit submitted by the Ad Hoc Committee in connection with consideration of the Sanctioning of the Plan read as follows:

> The Ad Hoc Committee has indicated to Goodmans, JPMorgan and Purdy Crawford personally on many occasions that the Ad Hoc Committee respects the fact that those entities and other organizations and individuals have expended an enormous amount of effort and have brought a great amount of skill to bear in designing the Plan and that

pursue a claim in fraud — a type of claim which (as it should be, of course) is extremely difficult to make out. As already noted, the decision of the Asset Providers to forego collapsing the derivative contracts held by them and realizing on the assets pledged to them by the Trusts was consensual and could be revoked at any time. Their decision, in that regard, was still playing out against a backdrop of historically volatile credit markets. There was a real risk that the Asset Providers would walk away from the process if we — or anyone else — successfully opposed the formulation of the Plan as it had been presented and voted on.[48] In short, on many memorable days, it was very hot in the kitchen.[49]

However, after careful consideration and discussion, the position of the Ad Hoc Committee was that, in plain terms, it just did not seem — in the words of the *CCAA* — "fair or reasonable" to allow a *CCAA* plan to confer an unlimited release with respect to fraud in the circumstances of the ABCP case. Again, we acknowledged the exception of the *Muscletech* case; however, in that case, among other things, the drug had been illegal (and therefore off the market) and litigation had been ongoing for years by the time the *CCAA* proceeding started. Accordingly, in that case, it was highly unlikely that any further "smoking guns" or, for that matter, any legitimate new creditors were going to emerge by the time that parties were called upon to submit to the jurisdiction of the *CCAA* process, including the claims process. As such, in our submission, the issue of fraud in *Muscletech* became effectively moot, as discussed in footnotes 33 and 41.

Accordingly we argued that the release provisions of the Plan should not cover fraud.

As noted at the outset of this article, space limitations prevent doing full justice to all of the arguments made against our position (indeed, we are not even doing full justice to the presentation of our *own* position). Suffice to say that there were several parties to the right and left of our position as to the need for a fraud carve-out from the release. To the right of us, counsel for the Crawford Committee, the Canadian Banks and the Asset Providers (many of whom were foreign banks) argued that the unqualified release should stand on the basis that a Plan under the *CCAA* is essentially just a contract and thereby could include such a contractual

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there are many sensible, commendable and desirable features of the Plan. However, the Ad Hoc Committee and its advisors have also worked extremely hard since mid-February, 2008 to respond to the complex, detailed provisions of the Plan and have, in good faith, identified the fundamental issues and concerns of the Ad Hoc Committee set out in this affidavit, all of which are respectfully submitted.

48 There were numerous other pressures at work. For example, some ABCP holders — who were not members of the Ad Hoc Committee — argued strongly and eloquently against the releases but then settled, out of court, with the institution who sold them their ABCP and withdrew from the fray.

49 We also knew that we could not ask Justice Campbell to rewrite the release provisions of the Plan. On a *CCAA* Sanction hearing it is neither fair nor appropriate to ask a Judge to do that. Instead, we just had to argue it out ourselves on the basis that the Plan, including the release, either merited approval or it did not. There was no "safety zone" position to take refuge in.

term.[50] To the left of us, counsel for several corporate ABCP holders argued that the releases should be stricken from the Plan entirely on the basis that the purpose of the *CCAA* is to address compromises between (just) a debtor and its creditors — not the obligations of third parties. The parties to the left of us suggested the *Muscletech* case was wrongly decided and put forward the Quebec Court of Appeal decision in *Michaud v. Steinberg*[51] as authority for the proposition that a *CCAA* plan should not be allowed to confer a release on a third party in addition to the *CCAA* debtor.

(e) The Decision of Mr. Justice Campbell in Response to the Original Sanction Hearing

In his decision — released May 16, 2008 — Justice Campbell ruled that he was "not satisfied that the release proposed . . . to encompass release from fraud . . . is . . . properly authorized by the *CCAA*, or is . . . fair and reasonable."[52]

Justice Campbell held that the parties should report back to him by May 30, 2008, to report on proposals "if any, for resolving potential claims in fraud."[53]

(f) The Fraud Carve-out

Ultimately a fraud carve-out was put forward by the Applicants in accordance with our core position on May 12 and 13, 2008. We engaged in some very intense, time limited negotiations over the terms of this carve-out and it was amended further before the Plan, including this amended fraud carve-out, came back before Justice Campbell on June 3, 2008.

Under the terms of the carve-out:

- No member of the Crawford Committee was entitled to assert a claim.
- The fraud to be complained of had to be wilful and direct and needed to have been focused on specific representations made to a buyer of ABCP at the time of the purchase. Accordingly, the carve-out was effectively limited to claims against ABCP dealers.

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50 It was also argued by the Canadian and foreign Banks that, without the unlimited releases, a cascade of litigation, with numerous "claims over" would result. In that regard, among other things, Justice Campbell's decision may be noted:

> Fraud involves wilful conduct made directly to a party in circumstances that the representor knows are false, done for the purpose of inducing a contract to be entered into. Claims in fraud are of a personal nature (even if there may be vicarious responsibility) and by their very nature do not easily lead to third party claims or claims over, as do claims in negligence.

See *ATB Financial*, *supra*, n. 37 at para. 35.

51 *Michaud v. Steinberg* (1993), 42 C.B.R. (5th) 1 [*Steinberg*].

52 *ATB Financial*, *supra*, n. 37 at para. 10. Justice Campbell held that the Plan could legitimately release negligence.

53 *Ibid.*, at para. 40.

- The carve-out did not contemplate claims over. (This provision was arguably of benefit to plaintiffs in that it precluded them from being met with multiple defences. See also footnote 50.)
- There was no process whereby a claimant needed to get leave of the Court to pursue his or her claim. However, the time limit for asserting the claims was relatively tight. We negotiated an extension of this deadline from 6 to 9 weeks from the making of the sanction Order.
- The carve-out precluded claims for consequential or punitive damages.
- With reference to our long standing core submission that it was inappropriate to ask ABCP holders to forego claims based on facts of which they were unaware, the carve-out was not designed to allow for claims based only on broadly applicable facts that might emerge in the future, but were not currently in the public domain.

It is to be noted that the Banks did not seek to amend any of the enhanced margin facility arrangements at the time that the fraud carve-out was added to the Plan.

In addition to negotiating for an extension of the time for filing claims, we negotiated changes with respect to the posting of security for costs and so as to allow for the further particularization of a pleading based on facts gathered through the discovery process.

(g) The Second Sanction Hearing and Justice Campbell's Decision in Support of the Plan

Having negotiated the terms of the fraud carve-out to the best of our ability in the circumstances, we supported the sanctioning of the Plan with the carve-out.

The matter came back before Justice Campbell and, despite continued strong opposition from a group of ABCP holders to the left of us, he sanctioned the Plan at this stage.[54]

In so doing, Justice Campbell noted the evolution of the position of the Ad Hoc Committee:

> . . . as this matter has progressed, additions to the supporter side have included for the proposed releases the members of the Ad Hoc Investors' Committee. The Ad Hoc group had initially opposed the release provisions. The Committee members account for some two billion dollars' worth of Notes.[55]

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54 *Ibid.* Numerous parties continued to oppose the sanctioning of the plan. In the kind of odd situation which only the English language seems capable of producing it may be noted that there are two very distinct, contradictory meanings of the word "sanction": (i) permission or approval; but also (ii) penalty imposed. In the U.S. Court system a "sanction hearing" is not (as it is in Canada) an "approval" hearing; it is an occasion for the imposition of a penalty.

55 *Ibid.*, at para. 51.

Justice Campbell also spoke to the issue of parties being asked to release claims based on facts which they were unaware of at the time in question:

> I leave to others the questions of all the underlying causes of the liquidity crisis that prompted the [ABCP] Note freeze in August, 2007. If by some chance there is an organized fraudulent scheme, I leave it to others to deal with.[56]

(h) The Appeal

A number of dissident ABCP holders appealed Justice Campbell's sanction Order and the matter came before the Court of Appeal for two full days of argument on June 25 and 26, 2008.

(i) The Decision of the Court of Appeal

The Court of Appeal decision was rendered on August 18, 2008.

The Court of Appeal held that a *CCAA* Plan may contain a release of claims against someone other than the debtor company or its directors and that Justice Campbell had not erred in the exercise of his discretion to sanction the Plan in this case, given the nature of the releases called for under it (and which, of course, now included a fraud carve-out).

Justice Blair rejected the decision of the Quebec Court of Appeal in *Michaud v. Steinberg* and held that a *CCAA* plan can include releases of third parties "where those releases are reasonably connected to the proposed restructuring."[57] Justice Blair stressed the connection between what the banks and the asset providers were giving — in the form of their contributions to the plan — and what they were receiving in the form of the releases. Of course, as already noted, the releases benefited a much wider group of parties than those who were making specific contributions to the Plan.

With respect to the delicate issue of fraud[58] Justice Blair held:

> The law does not condone fraud. It is the most serious kind of civil claim . . . [o]n the other hand . . . there is no legal impediment to granting the release of an antecedent claim in fraud, *provided the claim is in the contemplation of the parties to the release at the time it is given.*[59]

(j) Application to the Supreme Court of Canada

Somewhat surprisingly, leave to appeal the decision of the Court of Appeal was denied by the Supreme Court of Canada on September 19, 2008.

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56 *Ibid.*, at para. 127.

57 *Steinberg, supra*, n. 51 at para. 43.

58 Note that it was Justice Blair, as he then was, of the Ontario Court (General Division) who stated that "fraud unravels all." *Frasmet Holdings, supra*, n. 45.

59 (2008), 45 C.B.R. (5th) 163 at para. 111 [emphasis added]. Query the extent to which anyone can be said to be "contemplating" a claim based on fraudulent activity that they are unaware of and could not possibly be aware of? Again it was our view that in the *Muscletech* type of situation that question was effectively moot.

6. NEW SENIOR FUNDING FACILITIES AND THE PUSH TO PLAN IMPLEMENTATION

As things turned out, there was still quite a bit of road to travel after that decision of the Supreme Court.

The Applicants strove to complete the closing of the restructuring transaction in the early fall of 2008, but multiple extensions were announced as a result of "current market conditions, the complexity of the restructuring and the large number of participants involved."[60]

In December, 2008, it was announced that the Applicants had also sought out and obtained, significant additional support to the Plan. These final enhancements to the Plan included:

- the introduction of a moratorium period ("Moratorium Period") of 18 months from the plan implementation during which collateral calls on certain credit default swaps would be prohibited;
- the further relaxing of certain critical spread loss triggers, so as to make the likelihood of those triggers being reached after the Moratorium Period more unlikely; and
- the provision of an additional $3.45 billion senior ranking "back stop" margin funding facility to be provided by a combination of Canadian governments (the Federal Government, the Government of Ontario, the Government of Alberta and the Government of Quebec), available to be used for a period of one month following the expiry of the Moratorium Period if the other margin facilities are exhausted.

These enhancements were enough to obtain an A rating, from DBRS, for the new senior paper.

On January 12, 2009, the Ontario Superior Court made a comprehensive Implementation Order designed to allow for closing of the final form of the transaction, incorporating the enhancements obtained in December, 2008. The final closing occurred in January, 2009.

7. CONCLUSION

It is now beyond dispute that, as a matter of Canadian law, a *CCAA* plan may validly contain third party releases. However, it remains to be seen just how far this practice will be applied in any particular case. Third party releases can only be justified in rare cases. Even in those rare cases, it may be that the releases will not be able to go so far as to absolve parties from liability for at least some degree of fraud.

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60 Fifteenth Report of the Monitor (26 November 2008) at para. 77.