

Financial Services Flash

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*The Futura Loyalty Group Inc. (Re):*¹ Cost-Benefit Analysis of Meeting Pre-Filing Customer Obligations Under the CCAA

In October 2012, The Futura Loyalty Group Inc. (“Futura”) commenced proceedings under the *Companies’ Creditors Arrangement Act* (the “CCAA”). On November 13, 2012, Justice Brown of the Ontario Superior Court of Justice (Commercial List) (the “Court”) considered Futura’s request to permit pre-filing, pre-payment obligations to its key customers.

Futura’s primary business is the provision of a customer rewards program. Approximately 70% of Futura’s total business is accounted for through the sale of Aeroplan Miles to merchants who, in turn, provide the Aeroplan Miles to their customers. Some merchants pre-pay for Aeroplan Miles at a discount to the price they would normally pay. Any claims related to the pre-payment for Aeroplan Miles by merchants would be considered unsecured claims and those merchants would not receive any benefit or payment ahead of Futura’s secured creditors.

With the support of its secured creditors and the Court-appointed monitor, Futura requested the Court’s approval to honour the existing commitments to Futura’s pre-paid merchants. The result would be to maintain the status quo of Futura’s business by preserving its relationship with important customers and safeguarding its brand in the marketplace.

Citing both *Eddie Bauer of Canada Inc.*² and *EarthFirst Canada Inc.*,³ Justice Brown found that the request by Futura was analogous to permitting payments to critical suppliers – a practice made possible under section 11.4 of the CCAA. In each of those cases, payment to critical suppliers was permitted in order to prevent disruption to the business and to maximize the value of the company for its creditors. Justice Brown noted that these cases employed a proportionality test, which analyzed the cost of the payments to the critical suppliers against the benefits to the debtor company and its creditors.

Justice Brown employed a similar cost-benefit analysis in determining whether to permit Futura to honour its commitments to the pre-paid merchants. The expected revenues from these customers totaled approximately \$440,000, whereas the cost of honouring the pre-paid commitments was approximately \$108,000. Brown J. also considered the significant proportion of Futura’s total revenues generated through the sale of Aeroplan Miles and noted that a failure to meet existing commitments would likely jeopardize the operation of the company as a going concern.

In the result, Justice Brown found that the benefit to Futura and its creditors from maintaining relationships with Futura’s key customers outweighed the costs to its creditors associated with honouring the pre-paid commitments. Accordingly, Justice Brown approved the request to honour pre-filing, pre-paid obligations to Futura’s key customers.

The consideration of honouring pre-filing obligations to key customers was not necessarily a novel issue for the Court. Justice Morawetz considered pre-filing obligations, including those to key customers, in *Cinram International Inc. (Re)*,⁴ where he held that honouring pre-filing obligations to customers would maximize the value for all creditors. However, Morawetz J. did not articulate how he reached that conclusion. The reasons provided by Justice Brown in Futura provide clarity and is authority for the proposition that certain pre-filing obligations to a debtor company’s key customers may be approved in the context of CCAA proceedings if the overall benefits of doing so outweigh the costs to the debtor company and its creditors.

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1 [2012] O.J. No. 5362 (ONSC).
2 2009 CanLII 32699 (ONSC).
3 2009 ABQB 78.
4 [2012] O.J. No. 3034 (ONSC)