Proactive Super-Priority of DIP Lenders Prevails over Reactive Post-Filing Creditors

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The Quebec Court of Appeal’s unanimous decision in *Gestion Éric Savard* reaffirms the super-priority ranking of CCAA DIP financing over regular unpaid post-filing obligations, absent steps being taken to reverse this usual order of priorities.

The debtor companies in *Gestion Éric Savard* (collectively, the “Debtors”) operated a network of optometry clinics in Quebec and Ontario. In May 2017, the Debtors sought protection under the CCAA and obtained an initial order thereunder (the “Initial Order”), and Raymond Chabot Inc. was appointed by the Quebec Superior Court as the Debtors’ monitor (the “Monitor”).

Pursuant to section 11.2 of the CCAA, the Initial Order permitted the Debtors to borrow up to $4,500,000 from Fiera Financement Privé inc. (the “DIP Lender”) as DIP financing, and, as security for such DIP financing, granted the DIP Lender a priority security interest over all the Debtors’ property (the “DIP Lender’s Charge”). After the issuance of the Initial Order, a number of the Debtors’ creditors, including landlords and equipment lenders (the “Specified Post-Filing Creditors”), raised concerns about non-payment for post-filing services that they were providing to the Debtors.

As part of an August 2017 motion brought by the Monitor to approve certain “outside the normal course of business” sale transactions of the Debtors’ property, the Specified Post-Filing Creditors claimed rights over the proceeds realized from such sale transactions and asked that the Monitor be directed by the motion Judge to distribute the proceeds first to the Specified Post-Filing Creditors, in priority to the DIP Lender and any other secured creditor. The Honourable Justice Jean-François Émond approved the sale transactions, but did not decide the priority dispute between the DIP Lender and the Specified Post-Filing Creditors, instead ordering that the Monitor hold $750,000 in trust from the sale proceeds (the “Trust Funds”) to pay post-filing creditor claims, which Trust Funds could only be released pursuant to a further Order.

In October 2017, the Monitor brought a motion for guidance as to whom the Trust Funds should be distributed. At first instance, The Honourable Justice Guy de Blois dismissed the DIP Lender’s argument that it was entitled to the Trust Funds in priority to all other creditors as a result of the DIP Lender’s Charge. Instead, His Honour held that the Specified Post-Filing Creditors should be paid “in priority to any other payment,” and established a distribution scheme for the Trust Funds to reflect this conclusion.

The DIP Lender appealed, which appeal was allowed unanimously by a three-Judge panel of the Quebec Court of Appeal. The panel noted that none of the Specified Post-Filing Creditors had been deemed a critical supplier and received a corresponding critical supplier charge under section 11.4 of the CCAA, the result of which was that none of the Specified Post-Filing Creditors had been compelled to extend credit to the Debtors. Similarly, the panel also noted that there is no inherent priority ascribed to post-filing creditors under the CCAA and that none of the Specified Post-Filing Creditors had brought a motion to amend the Initial Order to provide for a priority charge in their favour.

As such, the appellate panel relied on the reasoning enunciated in *Smoky River Coal*, namely, that CCAA initial orders are roadmaps upon which stakeholders rely to navigate CCAA proceedings, and stakeholders must therefore be able to look to the Initial Order to understand the benefits or security to which they are entitled and to which they are not entitled. In *Gestion Éric Savard*, the DIP Lender had relied on the protections afforded to it under the Initial Order by the DIP Lender’s Charge when it advanced financing throughout the CCAA proceedings, trusting that its super-priority position would not be altered by...
later claims of subsequently-ranked creditors. Accordingly, the Trust Funds realized from the Debtors’ property were to be distributed first to the DIP Lender.

_Gestion Éric Savard_ serves as a reminder that CCAA stakeholders are often most successful when their strategies are proactive and not reactive. As such, stakeholders should understand and assert their rights from the commencement of CCAA proceedings. For example, the Specified Post-Filing Creditors could have insisted upon receiving payment in cash at the time of supplying post-filing goods and services, or could have proposed that the extension of credit be conditional on go-forward priority rankings being modified. Accordingly, while the appellate decision in _Gestion Éric Savard_ is certainly favourable to DIP lenders on the surface, and while hindsight is always 20/20, the practical outcome could have been different for the DIP Lender and the Specified Post-Filing Creditors if the latter had not waited for the train to leave the station before entering the fray (which train often departs quickly in CCAA proceedings).

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1 _Arrangement relatif à Gestion Éric Savard inc., 2019 QCCA 1434 [Gestion Éric Savard]._

2 _Companies’ Creditors Arrangement Act, R.S.C., 1985, c. C-36., as amended [CCAA]._

3 Debtor-in-possession financing [DIP financing], also known as interim financing.

4 The Honourable Justices Doyon, Rancourt and Ruel.

5 _Montreal Trust Co. of Canada Ltd. v. Smoky River Coal Ltd., 2001 ABCA 209 [Smokey River Coal]._

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