

focus

on

Insolvency Law

February, 2008

The logo for Fraser Milner Casgrain LLP, consisting of the letters 'FMC' in white on a dark blue square background.

FRASER MILNER CASGRAIN LLP

ALBERTA COURT FINDS A DIP CHARGE CAN BE GRANTED IN PRIORITY TO THE DEEMED TRUST CLAIMS OF CRA

In *Re Temple City Housing Inc.; Minister of National Revenue v. Temple City Housing Inc.*, 2007 CarswellAlta 1806 (Alta. Q.B.), Temple City Housing Inc. ("Temple") filed for protection under the *Companies' Creditors Arrangement Act* ("CCAA"). The Order sought by Temple contemplated that a Debtor-In-Possession credit facility ("DIP Charge") would be granted. Temple's major creditor, Canada Revenue Agency ("CRA"), opposed the granting of the DIP Charge, which would create a court ordered priority over the CRA deemed trust claim.

CRA argued that its net claim of approximately \$720,000 should not be subordinated to the DIP Charge, arguing that Temple was undercapitalized, and that its business was too unpredictable. Moreover, CRA argued that the deemed trust arising pursuant to s. 227(4.1) of the *Income Tax Act* created a property interest in favour of CRA, which prevented CRA's claim from being superceded by the super-priority of a DIP Charge.

Romaine J. rejected the CRA's argument that the deemed trust created a property interest and referenced the Monitor's argument that the deemed trust claim was a security interest, albeit one that takes priority over other security interests - an interpretation supported by the definition of "security interest" in the *Income Tax Act* itself, which includes a reference to a "deemed or actual trust".

Romaine J. held that it is clear that a court in a CCAA proceeding is able to grant a super-priority over existing security interests for DIP financing, and she was satisfied that, in this case, Temple required the protection of the CCAA if there was to be any possibility that it would be able to continue in business for the benefit of its creditors, employees and other stakeholders. She was also satisfied that the DIP Charge of \$300,000 was both necessary and in the best interests of the company's stakeholders generally. Accordingly, the DIP Charge was approved.

It is interesting to note the circumstances surrounding the Order of

the Court of Queen's Bench. CRA was the debtor's largest creditor, being owed approximately \$970,000 in respect of un-remitted source deduction and GST. The DIP facility was only advanced to the extent of \$276,000 to fund for the immediate needs of the debtor, including its payroll and the related source deduction for the current pay period. Regardless of where proposed amendments provide for super priority DIP funding, the case is a good example of a DIP facility being used entirely simply to "keep the lights on".

CRA sought leave to appeal Romaine J.'s decision on the basis that she had erred in granting the DIP Charge over its deemed trust claims.

The Court of Appeal found that CRA was unable to meet the test for leave to appeal due to three factors:

1. The point which CRA sought to appeal would not be of significance to CCAA practice because the recently proposed amendments to the CCAA include specific authority to grant super-priority to DIP financing such as occurred in this case.
2. After Romaine, J. granted the Order, the DIP lender had advanced \$300,000 to Temple in reliance on the Order and, as the Order had not been stayed, the proceeds had been paid to Temple's employees and suppliers. Accordingly, it was now virtually impossible to "unscramble the egg".
3. An appeal would hinder the CCAA proceedings because, without the DIP order, the DIP lender would not advance funds and without current and future loans, Temple would be unable to restructure under the CCAA and would be forced to close its business.

Accordingly, the application for leave was not granted.

For further information please contact David Mann at (403) 268-7097 or David LeGeyt at (403) 268-3075, or visit our website www.fmc-law.com/insolvency