

Court of Appeal File No.:
Court File No.: CV-2300696017-00CL

COURT OF APPEAL FOR ONTARIO

IN THE MATTER OF THE *COMPANIES' CREDITORS
ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR
ARRANGEMENT OF LOYALTYONE, CO.

Applicant

NOTICE OF MOTION FOR LEAVE TO APPEAL

THE MOVING PARTIES, LoyaltyOne, Co. ("**LoyaltyOne**") and KSV Restructuring Inc. in its capacity as monitor of LoyaltyOne (and in such capacity, the "**Monitor**"), will make a motion to the Court of Appeal at Osgoode Hall, 130 Queen Street West, Toronto, on a date to be fixed by the Registrar.

PROPOSED METHOD OF HEARING: The Motion is to be heard in writing under rule 61.03.1(1) of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194 (the "**Rules**").

THE MOTION IS FOR:

- (a) an order granting leave to appeal to the Court of Appeal from the order of Justice Conway (the "**Motion Judge**") of the Superior Court of Justice (Commercial List) dated July 10, 2024 at Toronto (the "**Order**") which, among other things:
 - (i) prohibited LoyaltyOne from disclaiming the Tax Matters Agreement between Alliance Data Systems Corporation (now known as Bread Financial Holdings, Inc.) ("**Bread**") and Loyalty Ventures Inc. ("**LVI**") dated

November 5, 2021 (the “**TMA**”) under section 32 of the *Companies’ Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (“**CCAA**”); and

- (ii) denied that payment provisions under the TMA relating to a potential tax refund of approximately \$96 million (the “**Tax Refund**”) were a transfer at undervalue (“**TUV**”) under section 96(1)(b)(ii) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (“**BIA**”), as incorporated into section 36.1(1) of the CCAA;

(b) the costs of this motion; and

(c) such further and other relief as to this Honourable Court may seem just.

THE GROUNDS FOR THE MOTION ARE:

The Prospective Appeal Is Critical

The Decision Upends Settled Law Relating to Disclaimer

- (a) the Motion Judge’s decision prohibiting LoyaltyOne from disclaiming the TMA under section 32 of the CCAA, with support of the Monitor, fundamentally disturbs settled insolvency law by threatening to significantly restrict a CCAA debtor’s ability to use a key restructuring tool – disclaimer;
- (b) the Motion Judge prohibited disclaimer of the TMA because:
 - (i) it would “reverse the bargain that LoyaltyOne made” and allow it to “get out of the deal”, which the Motion Judge found was “not the intended purpose of a disclaimer under s. 32(4) of the CCAA”;

- (ii) it was “an attempt [by LoyaltyOne] to secure funds for itself that it was never entitled to retain” and “assist the Lenders in recovering the losses that they sustained on the transaction”, despite its effect being to maximize the value of LoyaltyOne’s estate for the benefit of creditors as a whole and to ensure the equitable treatment of creditors; and
 - (iii) it would prejudice Bread, solely because Bread would not receive the payment it expected;
- (c) however, these are some of the very reasons disclaimer is upheld, not denied, in settled CCAA caselaw;
- (d) in particular, it is a feature of every disclaimer in CCAA proceedings that the debtor is able to “reverse the bargain” and “get out of the deal” in an attempt to “secure funds for itself that it was never entitled to retain” in accordance with the purposes of the CCAA, including maximizing the value of its estate for the benefit of creditors and ensuring the equitable treatment of creditors, with the counterparty not receiving what it bargained for as a result;
- (e) contrary to the Motion Judge’s findings, those are in fact the clear and unequivocal purposes of disclaimer under the CCAA, which protect the interests of creditors as a whole;
- (f) the Motion Judge also prohibited the disclaimer because LoyaltyOne partially performed under the TMA prior to the CCAA filing;
- (g) however, section 32 of the CCAA and the applicable case law do not contain any such prohibition;

- (h) moreover, a partially performed agreement is precisely the type of agreement that a debtor would seek to disclaim, and it is the type of agreement disclaimed in virtually all CCAA proceedings;
- (i) the Motion Judge erred in law by holding that section 32 of the CCAA could not be used for its clearly intended and well-understood purposes in respect of an agreement to which disclaimer is intended by statute to apply;
- (j) the Motion Judge also erred in law by focusing solely on the secured lenders' rights, and failing to consider creditors as a whole, including unsecured creditors, when assessing disclaimer;

The Decision Redefines "Insolvent Person", Contrary to Statute

- (k) the decision by the Motion Judge denying that the TMA payment provisions relating to the Tax Refund are a TUV is also contrary to insolvency law, creates significant uncertainty in the practice, and contains errors of law as set out herein;
- (l) the Motion Judge employed an analysis of the debtor which ascribed an incorrect meaning to the term "insolvent person" under section 2 of the BIA;
- (m) as a result, the Motion judge (i) failed to include or account for a USD\$675 million guarantee given by LoyaltyOne as an "obligation due and accruing due", (ii) failed to have regard for the outcome of a contemporaneous sales process as a "fairly conducted sale under legal process", and (iii) failed to have regard to the balance sheet values of LoyaltyOne's assets and liabilities;
- (n) in doing so, the Motion Judge significantly narrowed the applicable grounds for finding that a debtor company is insolvent, contrary to the clear intention and

express definition contained in the BIA and applicable to the CCAA, which was an error of law;

- (o) the Motion Judge's decision with respect to disclaimer and TUV cannot be reconciled with the statutory language used in the BIA or the CCAA, or the overall scheme and purpose of the CCAA itself;

Background

- (p) on November 5, 2021 (the "**Spin Date**"), Bread implemented a spin-out of its subsidiary, LoyaltyOne, and another subsidiary, (the "**Spin Transaction**") which resulted in:
 - (i) the spin-off of LVI as an independent public company that would hold certain of Bread's subsidiaries, including LoyaltyOne;
 - (ii) LVI entering into a loan agreement to borrow USD\$675 million in term loans, together with a revolving facility for working capital and other corporate purposes in the amount of an additional USD\$150 million;
 - (iii) the requirement that LVI transfer substantially all of the term loan proceeds to Bread at closing to improve Bread's financial position;
 - (iv) LoyaltyOne "guaranteeing" the loan to LVI as primary obligor, with joint and several liability for the full amount of the debt together with the other guarantors – but with those guarantors having no capacity to pay, leaving LoyaltyOne with the exclusive ability to service the debt; and
 - (v) the distribution of approximately 80% of LVI's shares to Bread's shareholders, with Bread retaining approximately 19% of LVI's shares;

- (q) the Spin Transaction was implemented through a series of agreements, including the TMA – which, among other things, requires LoyaltyOne to pay an amount equal to the Tax Refund to Bread in the future, if and when it is received;
- (r) on the Spin Date, LoyaltyOne was an “insolvent person” as defined by section 2 of the BIA but was nevertheless obliged thereafter to make dividend payments to LVI to service its USD\$675M in debt and corporate costs because LVI had no operations of its own and no other means of funding the debt;

The CCAA Proceedings

- (s) LoyaltyOne suffered significant financial decline and commenced CCAA proceedings on March 10, 2023 (the “**CCAA Proceeding**”);
- (t) through a sale and investment solicitation process, LoyaltyOne sold substantially all of its operating assets, including the AIR MILES rewards program it had operated since inception, to affiliates of BMO;
- (u) LoyaltyOne’s remaining assets – which are insufficient to repay its creditors – consist of (i) the undistributed remaining net proceeds from the sale of its assets and cash on hand, and (ii) the amount of the Tax Refund, if received;
- (v) on October 27, 2023, LoyaltyOne provided Bread with a notice of disclaimer of the TMA under section 32 of the CCAA because Bread asserted entitlement to the Tax Refund for its own benefit notwithstanding that LoyaltyOne was subject to the CCAA proceedings and was advancing the Tax Dispute (as defined below) using funds that would otherwise have been available to LoyaltyOne’s creditors;

- (w) LoyaltyOne's creditor pool is composed of secured and unsecured debt, and Bread is an unsecured creditor;
- (x) the trial in the proceedings by LoyaltyOne against the CRA to determine whether LoyaltyOne is entitled to receive the Tax Refund (the "**Tax Dispute**") is scheduled to begin in September 2024;

The Proposed Appeal

- (y) on June 13 and 14, 2024, the Motion Judge heard a motion by Bread and a motion by LoyaltyOne and the Monitor, both for certain relief relating to the TMA;
- (z) among other things, the Motion Judge:
 - (i) prohibited LoyaltyOne from using section 32 of the CCAA to disclaim the TMA; and
 - (ii) denied that payment provisions under the TMA relating to the Tax Refund were a TUV pursuant to section 96(1)(b)(ii) of the BIA, as incorporated into section 36.1(1) of the CCAA;
- (aa) if leave is granted, this Court will be asked to answer the following questions:
 - (i) with respect to the disclaimer:
 - 1) Did the Motion Judge err in law by eliminating or restricting the statutory tool of disclaimer in a liquidating CCAA, contrary to Parliament's intention concerning section 32 and the CCAA generally, and binding case law?

- 2) Did the Motion Judge err in law by failing to consider the interests of creditors other than Bread and the secured lenders, who would substantially benefit from the disclaimer?
- (ii) with respect to determining whether the payment provisions in the TMA regarding the Tax Refund were a TUV:
- 1) Did the Motion Judge err in law by incorrectly interpreting and applying the definition of “insolvent person” in section 2 of the BIA, thereby narrowing the applicable grounds for finding that a debtor company is insolvent, contrary to the clear intention and express definition contained in the BIA?
 - 2) Did the Motion Judge make a palpable and overriding error in finding “[t]here is no analysis of how the debt was allocated among the three companies and whether the portion allocated to LoyaltyOne exceeded its fair market value”?

The Disclaimer Issue Satisfies the Test for Leave to Appeal

The Point on Appeal Is of Significance to the Practice

- (bb) the correct interpretation, application, and indeed availability of section 32 of the CCAA is of significance to insolvency practice because disclaimer in accordance with section 32 has a critical impact on CCAA proceedings generally and on the recovery available to a debtor company’s creditors specifically;
- (cc) Parliament’s intent for section 32 of the CCAA is to take into account the interests of all creditors to ensure an equitable result dictated by the guiding principles of

the CCAA, including maximizing available recoveries for all stakeholders, by properly applying the non-exhaustive factors set out in section 32(4) of the CCAA;

- (dd) if the Motion Judge's decision is left undisturbed it will eliminate or significantly restrict the availability of disclaimer as a tool available to a CCAA debtor company to maximize recoveries available to its creditors;

The Point Raised Is of Significance to the Proceeding

- (ee) the correct interpretation and application of section 32 of the CCAA is of significance to this proceeding because disclaimer of the TMA will result in up to \$96 million becoming available to maximize recovery for all of LoyaltyOne's creditors, rather than Bread alone, if LoyaltyOne succeeds in the Tax Dispute;
- (ff) overturning the Motion Judge's decision to prohibit disclaimer of the TMA would have a material effect on the outcome of this proceeding;

The Appeal Is Prima Facie Meritorious

- (gg) the proposed appeal is *prima facie* meritorious because the Motion Judge made several errors of law based on an incorrect interpretation and application of section 32 of the CCAA and which also conflict with established authority;

The Appeal Will Not Unduly Hinder the Progress of the Proceeding

- (hh) the proposed appeal will not unduly hinder the progress of this proceeding because LoyaltyOne has already sold substantially all of its operating assets and the Tax Refund is not expected to become immediately available;

The “Insolvent Person” Issue Satisfies the Test for Leave to Appeal

The Point on Appeal Is of Significance to the Practice

- (ii) the correct interpretation of the definition of “insolvent person” under section 2 of the BIA is of significance to the practice because the Motion Judge’s analysis of insolvency based on that definition, if left undisturbed, will significantly narrow the applicable bases for finding that a debtor company is insolvent, contrary to the clear intention and express definition contained in the BIA;

The Point Raised Is of Significance to the Proceeding

- (jj) the point raised is of significance to this proceeding because the Motion Judge’s incorrect interpretation and application of the definition of “insolvent person” led the Motion Judge to halt the TUV analysis prematurely, rather than considering all of the applicable factors pursuant to section 96(1)(b)(ii) of the BIA;
- (kk) had the Motion Judge correctly interpreted and applied the definition of “insolvent person”, the Motion Judge may have determined that the payment provisions in respect of the Tax Refund under the TMA were a TUV and that the TMA was void and unenforceable as a result, leaving up to approximately \$96 million available to maximize recoveries for all of LoyaltyOne’s creditors, rather than Bread alone;

The Appeal Is Prima Facie Meritorious

- (ll) the proposed appeal is *prima facie* meritorious because the Motion Judge erred in law by incorrectly interpreting and applying the definition of “insolvent person” in section 2 of the BIA;

The Appeal Will Not Unduly Hinder the Progress of the Proceeding

- (mm) the proposed appeal will not unduly hinder the progress of this proceeding because LoyaltyOne has already sold substantially all of its operating assets and the Tax Refund is not expected to become immediately available;

Leave to Appeal Should Be Granted

- (a) the proposed appeal is founded on serious and arguable grounds that are of real and significant interest to the parties and it is in the interests of justice to grant leave to appeal;
- (b) rules 1.04, 1.05, 61.03.1 of the Rules;
- (c) sections 11, 13, 14, 32, 36.1(1) of the CCAA;
- (d) sections 2 and 96(1)(b)(ii)(A) of the BIA; and
- (e) such further and other grounds as counsel may advise.

THE FOLLOWING DOCUMENTARY EVIDENCE will be used at the Motion:

- (a) the orders and endorsements made in the CCAA Proceeding, including the Motion Judge's reasons for decision and the Order;
- (b) the record before the Motion Judge in connection with the motions heard June 13 and 14, 2024; and
- (c) such further and other evidence as counsel may advise and this Honourable Court may permit.

July 31, 2024

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TO: **THE SERVICE LIST**

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