Ontario Court of Appeal upholds approval of plan of arrangement despite employee objections

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In its recently issued decision in *NexJ Systems Inc. (Re),* 2023 ONCA 451, the Ontario Court of Appeal upheld an application judge's decision to finally approve a plan of arrangement that required employees to sell their shares and provided guidance on the scope of a judge's discretion when hearing an application to finally approve a plan of arrangement.

What you need to know

- The Court of Appeal upheld a decision approving a CBCA plan of arrangement over objections of employees who were shareholders and creditors.
- The Court confirmed that application judges have the discretion to determine issues summarily, in keeping with the expedient nature and purpose of an application for approval of a plan of arrangement. Fairness will not require an application judge to defer the determination of any issue to a trial in every case.
- The Court also agreed that a judge hearing an application for final approval has the jurisdiction to approve the sale of shares in a related corporation where it is "no stranger" to the proceedings.

The decision

This case involves a plan of arrangement put forward by NexJ Systems Inc. (the Plan). The Plan required the employees to sell their shares in NexJ Systems and NexJ Health Holdings Inc. to a third party, N. Harris Computer Corporation. In exchange, the employees received 55 cents per NexJ Systems share and 25 cents per NexJ Health share, as well as the forgiveness of the balance of the interest-free employee loans that NexJ Systems gave them to purchase their NexJ System shares in 2011 (the 2011 Agreements).

In order to finally approve a plan of arrangement under s. 192 of the *Canada Business Corporations Act*, RSC 1985, c C-44, the Court must be satisfied that:

- there has been compliance with all statutory and Court-mandated requirements;
- the application has been put forward in good faith; and
- the arrangement is fair and reasonable.[1]

At the motion for final approval of the plan, 36 former employees and shareholders of NexJ Systems and NexJ Health argued that the Plan was not reasonable because it breached the 2011 Agreements and foreclosed their claims against NexJ Systems relating to the 2011 Agreements, including for the alleged significant tax liabilities caused by the implementation of the plan.

Justice Penny of the Superior Court of Justice rejected these arguments, finding that the Plan was reasonable and that the employees had not raised an arguable case, and approved the plan.

The appeal

The employees appealed the decision on three grounds, namely that Justice Penny:

1. erred by deciding the merits of the employees' claims with respect to the 2011 Agreements and releasing them without a trial;
2. exceeded his jurisdiction under s. 192 of the CBCA by approving the forced sale of the employees' shares in NexJ Health (a separate corporation from NexJ systems); and,
3. misapplied the fair and reasonable test.

The Court of Appeal dismissed the employees' appeal and upheld Justice Penny's decision approving the Plan. It found that an application judge has the discretion to determine whether to summarily decide issues, where appropriate, and in this case, there was no procedural unfairness.

The Court of Appeal also concluded that Justice Penny had correctly interpreted the governing criterion of fairness and reasonableness in approving the plan. The judge determined that the 2011 Agreements allowed for the forced sale of shares and repayment of loans under a plan of arrangement and did not err in disregarding the appellants' evidence regarding the purpose and effect of the 2011 Agreements. Furthermore, the proposed release of all shareholder claims was fair and reasonable. It stated that the employees had acknowledged the tax implications of the 2011 Agreements at the time they were signed and had the opportunity to seek independent advice before signing them.

The Court of Appeal also rejected the argument that the application judge exceeded his jurisdiction by approving the sale of shares in NexJ Health, as it was related to NexJ Systems and is "no stranger to [the] proceedings." Its inclusion was a necessary part of the financing arrangements of the plan of arrangement which benefited the employees because it provided a further paydown of their loans.

Finally, the court found that the application judge correctly determined that the proposed plan of arrangement had a valid business purpose. The judge considered the financial circumstances of NexJ Systems and its attempts to address challenges and concluded that there were no viable alternative transactions. The appellants did not provide evidence to suggest otherwise.

For more information on the Ontario Court of Appeal's decision in *NexJ Systems Inc. (Re),* 2023 ONCA 451, please reach out to one of the key contacts listed below.

[1] *BCE Inc. Re*, [2008] 3 S.C.R. 560 at para. 137.

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