

CITATION: Re iMarketing Solutions Group, 2013 ONSC 2223
COURT FILE NO.: CV-13-10067-00CL
DATE: 20130415

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE COMPANIES') *Robert I. Thornton and Danny M. Nunes, for*
CREDITORS ARRANGEMENT ACT,) *the Applicants*
R.S.C. 1985, c. C-36, AS AMENDED)
) *Matthew P. Gottlieb, for Duff & Phelps*
AND IN THE MATTER OF A PLAN OF) *Canada Restructuring Inc.*
COMPROMISE OR ARRANGEMENT OF)
iMARKETING SOLUTIONS GROUP) *Virginie Gauthier and Daniel Pearlman, for*
INC. and the Companies referred to in) *Shotgun Fund Limited Partnership III*
Schedule "A"(the "Applicants"))
) *Clifton P. Prophet, for Canadian Imperial*
) *Bank of Commerce*

HEARD: April 12, 2012

NEWBOULD J.

[1] iMarketing Solutions Group Inc. ("IMSG") and a number of subsidiary corporations applied on April 12, 2002 for protection under the CCAA, at which time an Initial Order was granted containing several provisions. These are my reasons for the granting of the order.

[2] Prior to December 3, 2012, IMSG was a publicly traded company listed on the TSX Venture Exchange. On that date, IMSG voluntarily delisted its common shares from the TSX-V and began listing its common shares on the Canadian National Stock Exchange.

[3] IMSG is the direct or indirect parent company of twenty-two subsidiaries ("IMSG Group"). Seventeen of the subsidiaries along with IMSG comprise the Applicants in these proceedings.

[4] The applicants are one of the largest participants in the telemarketing and fundraising industry in North America. The applicants provide direct marketing solutions for not-for-profit organizations, political organizations and professional associations. The IMSG Group's core businesses include: (i) tele-fundraising and outreach; (ii) data development; (iii) direct mail fundraising and outreach; (iv) data management; (v) publishing; (vi) social media; (vii) secure caging (an industry term for the process or act of collecting donations, processing donor mail and depositing contributions to customer accounts); and (viii) marketing list rentals (the renting of donor lists to third parties in exchange for a fee).

[5] The IMSG Group's Canadian operations are located in the provinces of Ontario, British Columbia, Alberta, Manitoba, Quebec and New Brunswick. The IMSG Group's U.S. operations are located in the states of Wisconsin, Colorado, Pennsylvania, Missouri, Virginia, New Mexico and Florida. For the nine months ended September 30, 2012, the IMSG Group's Canadian operations accounted for approximately 57% of the applicants' gross margin while U.S. operations accounted for the remaining 43%. In 2013, the applicants' Canadian operations were expected to account for 53% of the total gross margin.

[6] As at April 5, 2013, the applicants employed approximately 1,143 employees (662 active employees and 481 on layoff) almost evenly divided between Canada and the U.S. The applicants' employees are not unionized and there are no pension plans in place.

[7] The applicants have a \$2 million loan facility with CIBC made to The Responsive Marketing Group Inc. ("RMG"), which is one of the applicants. That loan has been fully advanced. It is secured against the assets of IRMG and guaranteed by other subsidiaries.

[8] On October 12, 2012, IMSG obtained bridge loan financing in the amount of \$1.5 million. The bridge loan was provided by Shotgun Fund Limited Partnership III ("SF LP III") controlled by, among others, Michael Davis, a director and officer of IMSG. The purpose of the

bridge loan was to address short-term liquidity issues and to improve IMSG's financial position. The net proceeds from the bridge loan were used for general working capital and operational restructuring purposes.

[9] On December 4, 2012, IMSG completed a private placement offering of a secured convertible promissory note. The gross proceeds from the offering were \$3.5 million and the sole subscriber was SF LP III. The convertible note has a maturity date of December 4, 2015. IMSG granted SF LP III a security interest in all of its assets. The amount owing under the convertible promissory note is approximately \$3.8 million. The proceeds from the offering were used to repay the bridge loan and to fund the applicants' general working capital requirements.

[10] As at April 5, 2013, the most significant liabilities of the applicants, other than their indebtedness to CIBC, approximately \$2.0 million, and SF LP III, approximately \$3.8 million, are as follows:

	(\$millions)
Unpaid Statutory Withholdings	\$0.2
Tax Authorities	\$1.2
Trade Creditors	\$4.3
Estimated Severance Obligations (as at April 5, 2013)	\$0.9
Estimated Future Obligations Relating to Abandoned Facilities	\$0.8
Rental Arrears	<u>\$0.4</u>
	\$7.8

Insolvency and Stay

[11] The evidentiary record establishes that the IMSG Group is facing an intense liquidity challenge such that it cannot pay all liabilities as they become due, which liabilities include ongoing operating costs, as well as legacy costs incurred as a result of previous operational

restructuring initiatives already undertaken. These initiatives were implemented with a view to returning the business of the IMSG Group to profitability.

[12] The record also establishes that without an immediate stay of proceedings, the applicants' businesses cannot survive. The applicants are under increasing pressure from their creditors to pay outstanding accounts, including certain suppliers of goods and services that are critical to the ongoing operation of the applicants' businesses, and under constant threat from their landlords and critical suppliers who threaten to take enforcement actions to bar the applicants from their business premises and to discontinue the supply of goods and services necessary for the applicants to operate their businesses.

[13] While the IMSG Group has historically been profitable, generating positive net income of approximately \$2.3 million and \$232,000 as recently as the fiscal years ending December 31, 2009 and 2010, over the most recent twenty-four month period it has generally incurred significant losses and, at present, the applicants lack sufficient liquidity to continue operating their businesses. For the three months ended September 30, 2012, the IMSG Group generated a loss of \$3.3 million and negative EBITDA from continuing operations of \$2.4 million. For the nine months ending September 30, 2012, the loss generated was \$4.7 million and the negative EBITDA from continuing operations was \$3.0 million. Although the IMSG Group has not finalized its audited financial statements for the year ending December 31, 2012, it expects to report continued material losses from ongoing operations as well as additional restructuring costs and losses from discontinued operations. For the first quarter of 2013, it expects that the IMSG Group will continue to show negative EBITDA and net losses, although the magnitude of such losses is expected to be materially lower than the quarterly results in 2012. It is expected that the IMSG Group will generate positive cash flow from ongoing operations shortly following the commencement of these proceedings.

[14] Over the past two years, the applicants have taken steps to address the challenges facing them by implementing a number of initiatives to lower operating costs through process efficiencies and higher productivity. They commenced the implementation of a restructuring plan that was intended to transform their business and called for significant changes to the

applicants' corporate structure, operations and management to bring these together under a single operating model. The applicants' restructuring plan has taken longer than expected to implement and anticipated operating results have not been achieved, resulting in the applicants' costs being higher than expected and savings being delayed.

[15] I am satisfied from the record, including the report from the proposed Monitor, that an Initial Order and a stay under section 11 of the CCAA should be made. The applicants request that the stay apply as well to limited partnerships which form part of their business in light of the integrated nature of the business. Although the CCAA applies to corporations, there is authority that the stay may in appropriate circumstances be ordered to apply to limited partnership interests, particularly where the business interests of the applicant corporations are intertwined with the limited partnerships. See *Re Lehndorff General Partner Ltd.* (1993), 9 B.L.R. (2d) 275. Such is the case with the applicants, and the stay requested is ordered.

[16] It is to be noted that CIBC is subject to the stay. There is an issue, however, between the applicants and CIBC that needs to be addressed quickly and I understand that the parties are dealing with it. That has to do with whether the CIBC loan, once reduced by payments being made directly to CIBC by customers of one or more of the applicants, is to be increased to \$2 million. I understand that the applicants do not intend to compromise the rights of CIBC, including its security and collateral position, as a result of the proceedings and that the parties are working towards a mutually acceptable arrangement to that effect. In the circumstances CIBC has reserved its rights concerning the Initial Order, which it has not opposed based upon this understanding.

DIP financing

[17] The record indicates that the IMSG Group will require additional emergency funding in order to implement this restructuring. SF LP III has agreed to provide debtor in possession financing to the applicants up to the aggregate amount of \$1.0 million, subject to the applicants obtaining an Initial Order in this proceeding on the terms requested granting the DIP Lender a charge over all of the property, assets and undertaking of the applicants in priority to all creditors

except CIBC. The cash flow forecasts for the period April 15, 2013 to August 2, 2013 indicate that in the absence of the DIP financing, the applicants have insufficient cash to continue to operate and operations will cease immediately. This is the view of both the applicants and the proposed Monitor.

[18] After considering the factors set out in section 11.2 (4) of the CCAA, it appears that the DIP financing and charge appears reasonable and they are approved.

Administration Charge

[19] The applicants propose an Administration Charge of \$300,000 to secure payment of the fees and expenses of the applicants' counsel, the Monitor and its counsel and the CRO and its counsel. The proposed Monitor is of the view that the proposed charge is reasonable. It appears to me relatively modest and is approved. This charge will rank after the CIBC security and before the other charges approved in the Initial Order, including the DIP charge.

Director's charge

[20] The applicants also propose a Directors' Charge of \$1.3 million for any liabilities the directors and officers may incur after the commencement of these proceedings. The applicants estimate that the post-filing priority payables in respect of which the directors would have personal liability are approximately \$1.3 million based on payroll, payroll remittances, vacation pay and sales taxes and determination or severance payments that may be owing. The proposed Monitor has reviewed the calculations and is of the view that the Directors' Charge is reasonable in relation to the quantum of the estimated potential liability. The Directors' Charge is approved.

Chief Restructuring Officer

[21] The applicants propose that Mr. Upkar Arora CA, ICD.D, co-founder and Managing Director of Illumina, be appointed Chief Restructuring Officer. Illumina is an independent financial advisory firm that provides financial, operational and strategic advisory services to mid-sized businesses. IMSG retained Mr. Arora on September 24, 2012 as interim CFO upon the resignation of IMSG's previous CFO. It was expected that Mr. Arora's appointment would last

for three months during which time he would, among other things, assist IMSG's board of directors in selecting a new CFO. Mr. Arora has remained in the position of interim CFO and, in that capacity, currently oversees the financial affairs of the applicants both in Canada and the U.S.

[22] Mr. Arora has intimate knowledge of the Applicants' operations, financial status and efforts that have been undertaken by the applicants to restructure their business. The applicants believe that Mr. Arora's knowledge and experience will be an asset to them and will be of great assistance to the proposed Monitor in guiding the applicants through this restructuring process. A fee of \$75,000 per month has been agreed, plus a success fee on terms to be negotiated subject to court approval. The proposed Monitor believes that the monthly fee for Mr. Arora is reasonable and that absent his retention, professional fees would increase by at least the monthly fee payable to him. Mr. Arora is appointed as CRO and as an officer of the Court on the terms agreed between the applicants and Mr. Arora.

Cash management system

[23] The IMSG Group operates an extensive centralized cash management system integrated among the various entities and centrally managed from IMSG's head office in Toronto. Cash is transferred daily, as needed, among some 120 bank accounts of the operating entities at multiple financial institutions its uses in Canada and the U.S. as well as customer accounts controlled by the IMSG Group. The applicants wish to continue this method of financing the various businesses on a daily basis. The proposed Monitor believes that it is necessary that this existing cash management system be continued as doing so would avoid (i) delays in accounts receivable collections and accounts payable payments until new bank and credit card accounts were established; (ii) a distraction of management's limited resources and (iii) payroll payment disruptions. It would also reduce administrative costs and expenses. The proposed Monitor points out that the cash flow projections do not consider the impact of cash flow delays and such delays would result in a need for increased funding which is not presently available.

[24] The Initial Order will contain a provision that subject to the terms of the DIP facility, IMSG is authorized to make loans, advances or transfers of funds to any of the other IMSG Group entities in accordance with the cash management system and the DIP facility and the subsidiaries are authorized to repay funds previously advanced to them by IMSG from time to time in accordance with the cash management system and DIP facility. As well, there shall be an Inter-Company Charge on the property of IMSG Group.

Critical Suppliers and customers

[25] The applicants have identified certain critical suppliers who provide goods and services critical to the applicants' ongoing operations. As well there are customers who to whom remittances were not made as required. The applicants have proposed in the Initial Order authority to make payments to these customers and critical suppliers for pre-filing indebtedness in consultation with the Monitor as it is believed that without making such payments their businesses cannot survive. The monitor believes the payments are appropriate and necessary for a number of reasons, including the fact that customers regularly engage on a per-contract or per-service basis and would be expected to terminate or not renew their contracts if payment obligations to them were not honoured. The cash flow projections indicate that the applicants will have sufficient liquidity to make these payments over the next several weeks.

[26] The authorization to pay pre-filing amounts to critical suppliers is codified in section 11.4 of the CCAA. Pursuant to this section, the Court has the discretion to:

- (a) declare a person to be a critical supplier, if it is satisfied the person is a supplier of goods or services to the company and the goods or services are critical to the company's continued operations (s. 11.4(1));
- (b) make an order requiring the "critical supplier" to supply any goods or services specified by the Court to the company on any terms and conditions that are consistent with the supply relationship or the Court considers appropriate (s. 11.4(2)).

[27] The rationale for the enactment of section 11.4 is explained in the Industry Canada Clause by Clause Briefing Book as follows:

Companies undergoing a restructuring must be able to continue to operate during the period. On the other hand, suppliers will attempt to restrict their exposure to credit risk by denying credit or refusing services to those debtor companies. To balance the conflicting interests, the court will be given the authority to designate certain key suppliers as "critical suppliers". The designation will mean that the supplier will be required to continue its business relationship with the debtor company but, in return, the critical supplier will be given security for payment.

[28] The critical suppliers have been identified in the affidavit material of the applicants.

[29] It is appropriate that the Initial Order contain a provision that the IMSG Group will be permitted to make such pre-filing payments owing to customers and to suppliers as determined by the IMSG Group in consultation with the Monitor to be necessary to permit them to proceed with the restructuring.

Chapter 15 proceedings

[30] IMSG Group intends to commence proceedings under Chapter 15 of the U.S. *Bankruptcy Code* pursuant to which they will seek to have these CCAA proceedings recognized as a foreign main proceeding and the Initial Order enforced in the US. IMSG will be named as the Foreign Representative in respect of the application. This would appear appropriate in light of the cross-border scope of the business, assets and operations of the applicants. The applicants are of the view that the center of main interests of the IMSG Group is in Ontario for a number of reasons set out in paragraph 21 of the affidavit of Mr. Langhorne. The proposed Monitor shares that view. They may well be correct, but it must be recognized that it is the function of the receiving court in the United States to make the determination on the location of the COMI and to determine whether this CCAA proceeding is a "foreign main proceeding" for the purposes of Chapter 15. See *Re Cinram* (2012), 91 C.B.R. (5th) 46, per Morawetz J.

[31] The Initial Order signed on April 12, 2013 contains the provisions discussed in this endorsement.

A handwritten signature in black ink, appearing to read "W. Newbould J.", positioned above a horizontal line.

Newbould J.

Released: April 15, 2013

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AND IN THE MATTER OF A PLAN OF
COMPROMISE OR ARRANGEMENT OF
iMARKETING SOLUTIONS GROUP INC. and the
Companies referred to in Schedule "A"(the
"Applicants")

REASONS FOR JUDGMENT

Newbould J.

Released: April 15, 2013