Court file number	2403-15089
Court	Court of King's Bench of Alberta
Judicial Centre	Edmonton
	In the Matters of the *Companies' Creditors Arrangements Act*, R.S.C. 1985 c. C-36, as amended. And in the matter of a plan of compromise or arrangement of Freedom Cannabis Inc.
Document	**Minister's brief of law**
Address for service and contact information of party filing this document	**Department of Justice Canada** 300 EPCOR Tower, 10423 – 101 Street N.W. Edmonton Alberta T5H 0E7 Attention: George F. Bódy Telephone: 780-495-7595 Email: George.Body@justice.gc.ca File number:500202833

Application before the Honourable Justice Mah
on Tuesday April 29, 2025 at 2:00 pm MDST on the Commercial List

Overview

1. The Crown takes issue with only one aspect of the orders sought by Freedom Cannabis Inc. ("**Freedom**") in respect of its liability of $9,693,946.85 pursuant to the *Excise Act, 2001, namely* the release of the directors from their statutory liability under the *Excise Act, 2001*.

Court Order Impact on Crown

2. As a result of the decisions of Freedom's directors, the Crown has lost approximately $10 million in tax revenue, has been prevented from exercising its rights to collect the tax debt, has not been able to vote on plan of restructuring, and the company, the directors, and their senior secured creditor/prospective purchaser, now seek to foreclose the Crown's ability to pursue the directors for $4.7 million of that tax debt for which they are liable, on the basis it is appropriate to do so, threatening to kill the deal unless the Court accedes to their demand.

3. Freedom obtained protection from its creditors on August 8, 2024 by way of an Initial Order under the *Companies' Creditors Arrangements Act* (CCAA) granted by Mr. Justice Lema

4. As of that date, Freedom was and remains liable to the Crown for $9,693,946.85 pursuant to the *Excise Act, 2001*. It incurred this debt over 25 months, from August 2022 to August 2024.[1]

5. CRA holds $483,500 cash as security for the *Excise Act, 2001* account liability (approximately 5% of the debt). The Crown seeks to apply this security against the debt, which would require post-RVO Freedom to post new security in the prescribed amount as a statutory condition of retaining its licence under the *Excise Act, 2001*. In discussions with Freedom's counsel, the Crown understands Freedom does not contest CRA's application of the security amount against the *Excise Act, 2001* debt.

6. As of the date of the Initial Order, Freedom is also liable for $117,958.15 pursuant to the *Excise Tax Act* for GST.[2] CRA has no means to recover this debt, either from Freedom or from Freedom's directors.

7. According to affidavits sworn by Mr. Potestio in this proceeding, in 2023, Freedom lost $9,599,173.[3] For the seven month period from January 1, 2024 to July 31, 2024, Freedom's internal balance sheet showed its loss for the year to be $5,320,226.61.[4] As of February 17, 2025, Freedom had drawn $2.4 million on the $3.0 million DIP facility (excluding accrued interest, fees and expenses)[5] and required the DIP facility to be increased by $1.75 million to cover anticipated expenses for the Forecast Period (February 17, 2025 to May 18, 2025)[6]. The DIP facility was increased to $4.5 million by Order of Justice Lema on February 26, 2025.[7] Adding these figures, Freedom has tax losses of approximately $19.4 million for 2023, 2024 and 2025 (to date). The order sought by Freedom will preserve those tax losses.

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1 Affidavit of Debbie Mitchell, sworn February 24, 2025, paragraph 8.

2 *Ibid*., paragraph 7.

3 First Affidavit of Johnfrank Potestio sworn August 6, 2024, Exhibit C, (pdf page 76/231).

4 Ibid., (pdf page 83/231).

5 Fifth Report of the Monitor paragraph 25.

6 *Ibid*., paragraph 8(b).

7 Order (Stay Extension) of Lema J. 26 February 2025, paragraphs 4(a) and (c).

Freedom will be able apply those losses against future income (of up to $19.4 million) and pay no income tax.

8. Freedom has classified its liabilities to employees whose employment it will terminate for amounts owing on account of statutory notice, termination payments, common law notice or pay in lieu thereof, severance, vacation pay, benefits, bonuses or other compensation or entitlements of any kind ("**Employee Termination Costs**") as Excluded Liabilities to be transferred to the scapegoat corporation as Excluded Liabilities.[8] (The scapegoat corporation will be impecunious, with no assets.[9]) The Crown anticipates Freedom will seek an order deeming these employees to be employees of the scapegoat corporation so their claims for Employee Termination Costs will have to be paid by the Crown under the *Wage Earner Protection Program Act* (WEPPA), which pays qualified employees up to $8,800 each. The Crown will have no means to recover any of these payments. Additionally, if an employee's claim exceeds the WEPPA limit, the affected employee will simply have to bear the loss, with no recourse.

A – Director Releases

9. The Minister is not aware of any other creditors who have claims against the directors of Freedom. To determine whether it is appropriate to release the directors, the court should be aware of what liabilities it is releasing the directors from, and not simply grant them a *carte blanche* release in an information vacuum.

10. The Minister of National Revenue is mandated by Parliament to administer and enforce the *Excise Act, 2001*.[10] In the administration of the statute, Parliament directed the Minister to appoint, employ, or engage the persons necessary to administer and enforce the Act.[11] The Minister and the CRA are required by law both to assess the tax liability as set out in the Act and to collect the amounts assessed.

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[8] Affidavit of Johnfrank Potestio sworn February 18, 2025, Exhibit B (Stalking Horse Subscription Agreement), paragraph 10.5(c).

[9] The "Excluded Assets" transferred to the scapegoat corporation are in fact liabilities with $0 value.

[10] *Excise Act, 2001*, SC. 2002 c. 22, section 8.

[11] Ibid., section 9.

11. Pursuant to section 160 of the Act, every licensee under the Act (persons licensed to produce or sell alcohol, tobacco, or cannabis) must file a return every month, calculate the duty payable for the month, and pay that amount to the Receiver General.

12. Section 295 of the Act imposes joint and several liability upon the directors of a corporation which fails to remit amounts required by the Act. This liability includes outstanding tax amounts, plus interest at the prescribed rate:

> 295 (1) If a corporation fails to pay any duty or interest as and when required under this Act, the directors of the corporation at the time it was required to pay the duty or interest are jointly and severally or solidarily liable, together with the corporation, to pay the duty or interest and any interest that is payable on the duty or interest under this Act.

13. The evidence before the Court is that Freedom was liable to the Minister in the sum of $9,693,946.85 as of February 21, 2025.[12] Ms Mitchell's affidavit also sets out the history of the accrual of this tax liability, stretching out over 25 months, from August 2022 to August 2024 (when the CCAA Initial Order was pronounced August 8, 2024). Given the stay of proceedings imposed by this Court, CRA has not been permitted to attempt to collect any portion of this debt.

14. The relief sought by the company for approval of the credit bid of JL Legacy Ltd.'s subsidiary/nominee, 2644323 Alberta Ltd., to become the new, 100% shareholder of Freedom leaves no funds to be paid to the Minister (or any other unsecured creditor). The reverse vesting order sought by Freedom moves the *Excise Act, 2001* debt and all other unsecured debts to the newly formed scapegoat corporation ("**GarbageCo**"), which has no assets, nor will it ever have assets.

Statutory condition precedent for liability of directors satisfied.

15. The *Excise Act, 2001* requires the Minister of National Revenue to exhaust her remedies against the corporation before turning to the directors for the shortfall:

> 295(2) A director of a corporation is not liable unless
>
> (a) a certificate for the amount of the corporation's liability has been registered in the Federal Court under section 288 and execution for that amount has been returned unsatisfied in whole or in part;

[12] Affidavit of Debbie Mitchell, sworn February 24, 2025, paragraph 8.

> (b) the corporation has commenced liquidation or dissolution proceedings or has been dissolved and a claim for the amount of the corporation's liability has been proved within six months after the earlier of the date of commencement of the proceedings and the date of dissolution; or
>
> (c) the corporation has made an assignment or a bankruptcy order has been made against it under the *Bankruptcy and Insolvency Act* and a claim for the amount of the corporation's liability has been proved within six months after the date of the assignment or bankruptcy order.

16. On June 20, 2024, the Minister followed the steps set out in section 288 of the *Excise Act, 2001*, certifying $4,764,620.64 of Freedom's liability under that statute, producing the certificate to the Federal Court, and requesting a writ of seizure and sale (for use in Alberta) from that Court.

17. On April 11, 2025, Justice Harris granted an order allowing the Minister to take the steps necessary to fulfill condition (2)(a) of the statute, and the Minister has taken those steps. The writ issued by the Federal Court in action T-1669-24 was referred to a civil enforcement agency in Alberta and returned unsatisfied in whole.

18. Subsection 295(4) is the assessing provision, authorizing the Minister to assess the directors for the liability of the corporation. However, subsection 295(5) imposes a 2-year limitation period for the Minister to assess, running from the time the person ceased to be a director of the corporation.

19. All the conditions necessary to assess the directors for $4.7 million of the $9.7 million debt have been satisfied. The time for the Minister to assess the directors has not expired. However, because the ARIO prohibits creditors (including the Minister) from taking steps against the directors of Freedom, CRA has not issued notices of assessment to the directors.

20. In *BlueStar Battery Systems International Corp, Re*. 2000 CanLII 22678 (ON SC), Farley J. considered Canada Customs and Revenue Agency's opposition to a provision in the creditor-approved plan releasing the directors from liability for the GST debt of the company. Farley J. observed that CRA could not legally pursue the directors of BlueStar after the Court approved the CCAA plan, extinguishing BlueStar's liability for the GST debt, because CRA had not taken the requisite steps under section 323(2)(a) of the *Excise Tax Act* before the debt was extinguished. Paragraph 323(2)(a) of the *Excise Tax Act* parallels paragraph 295(2)(a) of the *Excise Act, 2001*, applicable in this case.

21. With the Court's permission, the Minister has taken the requisite step to be able to pursue the directors for $4.7 million of the $9.7 million debt. The Minister has not sought permission to certify the balance of the *Excise Act, 2001* debt or the *Excise Tax Act* (GST) debt, and will not be able to do so after the Court releases Freedom from these liabilities. The Minister will be able to pursue the directors for less than half of the tax debt the directors incurred.

The statutory test – Due Diligence

22. While the provincial superior courts have developed their own test to determine the propriety of releasing third parties (including directors) from liability, the Crown is not aware of any case in which a provincial superior court has considered the established jurisprudence of the Tax Court of Canada and the Federal Court of Appeal interpreting the directors' liability provisions of the tax statutes.

23. In *Soper* v. *R*, [1998] 1 F.C. 124, 1997 CanLII 6352 (FCA), Robertson JA reviewed the legislative history of section 227.1 of the *Income Tax Act*, upon which section 295 of the *Excise Act, 2001* is based. He noted that section 227.1 was enacted in 1982 to address two problems: first, the nonpayment of corporate taxes *per se*, and second, the non-remittance of source deductions withheld by employers from their employees' wages or salaries. He observed:

> As companies experienced difficult financial times, corporations and directors actively and knowingly sought to avoid the payment of taxes in a variety of ways.
>
> …
>
> Faced with a choice between remitting such amounts [source deductions] to the Crown or drawing on such amounts to pay key creditors whose goods or services were necessary to the continued operation of the business, corporate directors often followed the latter course. Such patent abuse and mismanagement on the part of directors constituted the "mischief' at which section 227.1 was directed.
> [citations omitted]

24. Parliament set out the only defence to a directors' liability assessment: due diligence:

> **Diligence**
>
> (3) A director of a corporation is not liable for a failure under subsection (1) if the director exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances.

25. The test is what steps the director took *at the time of the default to prevent the default*.

26. In *Buckingham* v. *Canada*, 2011 FCA 142 (CanLII), [2013] 1 FCR 86, the Federal Court of Appeal heard the Crown's appeal of the decision of the Tax Court of Canada that Mr. Buckingham was not liable under section 227.1 of the *Income Tax Act*, the parallel provision under that statute addressing unremitted source deductions. The Tax Court of Canada had dismissed Mr. Buckingham's appeal of an assessment under section 323 of the *Excise Tax Act* for a directors' liability assessment for outstanding GST owing by his corporation. Mr. Buckingham appealed that decision.

27. Justice Mainville (writing for the Court) noted one issue for the Court to consider was

> Can a successful defence under subsection 227.1(3) of the *Income Tax Act* or subsection 323(3) of the *Excise Tax Act* be sustained where the efforts of the directors are focussed on curing failures to remit rather than towards preventing such failures?:[13]

28. The Federal Court of Appeal confirmed its earlier decisions in *Corsano*[14] and *Ruffo*[15] that subsection 227.1(3) specifically targets the *prevention* of the failure by the corporation to remit the required amounts – that is, to demonstrate due diligence and escape liability, the directors must prove that they exercised the degree of care, diligence and skill required to *prevent* the failures (para. 33), not efforts made after the fact.

29. With respect to decisions by directors to pay other creditors instead of the Crown, the Court rejected this as a defence to liability:

> [49] … In circumstances where a corporation is facing financial difficulties, it may be tempting to divert these Crown remittances in order to pay other creditors and thus ensure the continuation of the operations of the corporation. It is precisely such a situation which both section 227.1 of the *Income Tax Act* and section 323 of the *Excise Tax Act* seek to avoid. The defence under subsection 227.1(3) of the *Income Tax Act* and under subsection 323(3) of the *Excise Tax Act* should not be used to encourage such failures by allowing a due diligence defence for directors who finance the activities of their corporation with Crown monies on the expectation that the failures to remit could eventually be cured.

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[13] *Buckingham* v. *Canada*, 2011 FCA 142 at para. 23.

[14] *Canada v. Corsano*, 1999 CanLII 9297 (FCA), [1999] 3 F.C. 173 (C.A.), at paragraph 35.

[15] *Ruffo v. Canada (Minister of National Defence)*, 2000 CanLII 15199, [2000] 4 C.T.C. 39 (F.C.A.).

30. In *Balthazard* v. *Canada*, 2011 FCA 331 (CanLII), another decision of the Federal Court of Appeal issued seven months after *Buckingham*, Justice Mainville restated the tests set out by the Court in *Buckingham*:

> [32] In *Buckingham*, this Court recently summarized the legal framework applicable to the care, diligence and skill defence under subsection 323(3), as follows:
>
> a. The standard of care, skill and diligence required under subsection 323(3) of the *Excise Tax Act* is an objective standard as set out by the Supreme Court of Canada in *Peoples Department Stores Inc.(Trustee of)* v. *Wise*, 2004 SCC 68, [2004] 3 S.C.R. 461. This objective standard has set aside the common law principle that a director's management of a corporation is to be judged according to his or her own personal skills, knowledge, abilities and capacities. However, an objective standard does not mean that a director's particular circumstances are to be ignored. These circumstances must be taken into account, but must be considered against an objective "reasonably prudent person" standard.
>
> b. The assessment of the director's conduct, for the purposes of this objective standard, begins when it becomes apparent to the director, acting reasonably and with due care, diligence and skill, that the corporation is entering a period of financial difficulties.
>
> c. In circumstances where a corporation is facing financial difficulties, it may be tempting to divert these Crown remittances in order to pay other creditors and thus ensure the continuity of the operations of the corporation. That is precisely the situation which section 323 of the *Excise Tax Act* seeks to avoid. The defence under subsection 323(3) of the *Excise Tax Act* must not be used to encourage such failures by allowing a care, diligence and skill defence for directors who finance the activities of their corporation with Crown monies, whether or not they expect to make good on these failures to remit at a later date.
>
> d. Since the liability of directors in these respects is not absolute, it is possible for a corporation to fail to make remissions to the Crown without the joint and several, or solidary, liability of its directors being engaged.
>
> e. What is required is that the directors establish that they were specifically concerned with the tax remittances and that they exercised their duty of care, diligence and skill with a view to preventing a failure by the corporation to remit the amounts at issue.

31. The Federal Court of Appeal revisited the issue again nine years later in *Ahmar* v. *Canada*, 2020 FCA 65 (CanLII).[16] The Tax Court of Canada dismissed Mr. Ahmar's appeal of his

[16] *Ahmar* v. *Canada*, 2020 FCA 65 (CanLII).

assessment for HST liability of his company, acknowledging that the company had been subject to a series of unfortunate events that it described as a "perfect storm", but finding that Mr. Ahmar's decision to use company funds to keep the company going rather than pay the HST did not relieve him of liability.[17] The Federal Court of Appeal cited its decisions in *Buckingham* and *Balthazard*, found no error in the Tax Court's decision, and dismissed Mr. Ahmar's appeal.

32. The jurisprudence from the Federal Court of Appeal interpreting the director liability provisions of the tax statutes is robust, well established, and has been well known and applied consistently for over 25 years. Notwithstanding this long-standing authority, the provincial superior courts have developed their own tests to release directors from liability apparently with no knowledge or acknowledgement of the Federal Court of Appeal's decisions.

33. The evidence tendered by Johnfrank Potestio in his affidavits demonstrates he and the directors made the very choice (repeatedly for 25 months) which Parliament condemned 43 years ago and enacted the director liability provision to address.

34. Mr. Potestio complains about the "draconian" regulatory regime and an increased taxation burden from excise taxes.[18] He asserts the effective tax rate on cannabis is 40%.[19] Cannabis sales are federally taxed on a fixed rate of $1/gram for sales up to $10/gram, and at 10% for sales over $10/gram. That is, if cannabis sells for $10/gram, the federal tax is $1 with an effective tax rate of 10%. If cannabis sells for $5/gram, the federal tax remains $1 with an effective tax rate of 20%. While Parliament and the provincial legislatures have enacted their respective tax rates, neither body controls the sale price of cannabis. That is dictated by the private market, where Freedom and its directors have chosen to conduct business.

35. Notably absent from the company's materials and the directors' materials is a *Notice of Constitutional Question*, challenging the validity of the *Excise Act, 2001* or the rates of

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[17] *Ibid*, at para 11.

[18] Affidavit of Johnfrank Potestio sworn April 21, 2025 (Osler, Hoskin & Harcourt LLP) para. 10

[19] *Ibid*., at para. 14.

taxation prescribed under that statute. Nor do they advance any legal argument demonstrating a flaw in the legislation. In the absence of any legal argument, the directors' assertions concerning the taxation of the cannabis industry can be summarized as "it's not fair".

Procedural Safeguards

36. If the Minister assesses a person pursuant to subsection 295(4) of the *Excise Act, 2001*, that person may file an objection to the assessment (*EA2001* s. 195) with the CRA, and if not satisfied with the decision of CRA's Appeals unit, may file an appeal with the Tax Court of Canada (*EA2001* s. 198). Parliament vested that Court with exclusive original jurisdiction to hear and determine appeals under many statutes including the *Excise Act, 2001*.[20] There is no prejudice to the directors addressing any assessments under the procedure prescribed by Parliament. They have the right to make full answer to the assessments before

Director Releases under the CCAA

37. The issue of the release of persons other than the debtor applicants under the CCAA goes back to 1993 and the Québec Court of Appeal's decision in *Michaud* v. *Steinberg* Inc., 1993 CanLII 3991 (QCCA). The Court decided that in the absence of specific statutory authority, the Court did not have authority to release persons other than the debtor companies (applicants) from liability. Parliament responded to the decision and enacted section 5.1 in 1997.[21]

38. Section 5.1 provides:

> **Claims against directors — compromise**
> 5.1 (1) A compromise or arrangement made in respect of a debtor company may include in its terms provision for the compromise of claims against directors of the company that arose before the commencement of proceedings under this Act and that relate to the obligations of the company where the directors are by law liable in their capacity as directors for the payment of such obligations.
>
> **Exception**
> (2) A provision for the compromise of claims against directors may not include claims that
> (a) relate to contractual rights of one or more creditors; or

[20] *Tax Court of Canada Act*, RSC 1985 c. T-2, s. 12.

[21] 1997, c. 12, s. 122

> (b) are based on allegations of misrepresentations made by directors to creditors or of wrongful or oppressive conduct by directors.
>
> **Powers of court**
> (3) The court may declare that a claim against directors shall not be compromised if it is satisfied that the compromise would not be fair and reasonable in the circumstances.
>
> **Resignation or removal of directors**
> (4) Where all of the directors have resigned or have been removed by the shareholders without replacement, any person who manages or supervises the management of the business and affairs of the debtor company shall be deemed to be a director for the purposes of this section.

39. As the CCAA was enacted by Parliament, a plan of arrangement proposed by a company to its creditors could include a release of directors from liability under s. 5.1. Under subsection 6(1) of the CCAA, a plan must be supported by the requisite majorities in number and dollar value of each class of creditors. With respect to the classification of creditors, the Québec Court of Appeal observed that creditors with claims against the company and the directors should be in a class distinct from creditors with claims against only the company, as the two groups have divergent interests, and the interests of the company+director class should not be overwhelmed by the company-only class.[22] Of course, applying this distinction, the plan would have to be approved by both the company+director class and the company-only class, effectively giving each class the power to reject the plan. Notably, Parliament authorized the Court to declare a claim shall not be compromised (despite being approved by the requisite majority of creditors) if it would not be fair and reasonable in the circumstances.

Metcalfe & Mansfield: a new test

40. The CCAA plan put forward in *Metcalfe & Mansfield Alternative Investments II Corp. (Re)*, 2008 CanLII 27820 and confirmed by the Ontario Court of Appeal ((2008), O.R. (3d) 513, 2008 ONCCA 587 (CanLII)) addressed the restructuring of the $32 billion non-bank sponsored portion of Canada's $116 billion asset backed commercial paper (ABCP) market. The applicants put forward a plan, voted on and well supported by all classes of creditors[23],

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[22] *Michaud* v. *Steinberg*, 1993 CanLII 3991 (QCCA), per Vallerand JA un-numbered paragraphs 4, 5.

[23] *Metcalfe & Mansfield*, Ont SCJ para 26.

which plan included a release of plan participants (who were not the applicants) from claims of negligence but not of fraud. The underlying issue was the Court's authority to approve such a plan, in the absence of a specific provision in the CCAA. While CCAA ss. 5.1(1) permitted the creditors to approve a plan providing for the release of the corporations' *directors* from liability (with the exceptions cited in CCAA ss. 5.1(2)), no provision in the CCAA permitted the release of third parties.

41. Justice Campbell concluded, at paragraph 143:

> [143] I have as a result addressed a number of questions in order to be satisfied that in the specific context of this case, a Plan that includes third party releases is justified within CCAA jurisdiction. I have concluded that all of the following questions can be answered in the affirmative.
>
> 1. Are the parties to be released necessary and essential to the restructuring of the debtor?
>
> 2. Are the claims to be released rationally related to the purpose of the Plan and necessary for it?
>
> 3. Can the Court be satisfied that without the releases the Plan cannot succeed?
>
> 4. Are the parties who will have claims against them released contributing in a tangible and realistic way to the Plan?
>
> 5. Is the Plan one that will benefit not only the debtor but creditor Noteholders generally?
>
> 6. Have the voting creditors approved the Plan with knowledge of the nature and effect of the releases?
>
> 7. Is the Court satisfied that in the circumstances the releases are fair and reasonable in the sense that they are not overly broad and not offensive to public policy?
>
> [144] I have concluded on the facts of this Application that the releases sought as part of the Plan, including the language exempting fraud, to be permissible under the CCAA and are fair and reasonable.

42. As noted, the release of the third parties was put to the creditors, who voted overwhelmingly to support it. This test was formulated in the extraordinary circumstances of the 2008 global financial crisis, providing protection for investors without resorting to a government bail-out.

43. With the disenfranchisement of creditors through the Courts' adoption of reverse vesting orders, the sixth factor in *Metcalfe* – creditors voting to approve the releases – has lost its relevance. The remaining factors all require the moving party to demonstrate – on the civil standard – the *necessity* of the releases to the viability of the company's proposed resolution of its debt problem.

44. In the present case, as far as the Minister knows, she is the only creditor with claims against the directors and is the only creditor affected by the release of the directors.

45. At the hearing before Lema J. on February 26, 2025, when Freedom applied for various orders including an order approving the Stalking Horse Subscription Agreement as the stalking horse bid, the Crown advised it would be opposing the release of the directors at the April 29th hearing. If JL Legacy's bid was contingent on the Court releasing the directors from liability, it was on notice to consider whether it would proceed with the bid if the Court did not release the directors.

Entrec Corporation (Re) **2020 ABQB 751 (CanLII)**

46. In *Entrec*, Romaine J considered eighteen factors in an application seeking the release of the directors of the corporation from liability despite the absence of a plan put to the creditors:

> (a) The directors and officers provided critical direction leading up to the filing of the present CCAA proceedings;
>
> (b) They were instrumental in administering the sale and investment solicitation process ("SISP") for the benefit of the Applicants' stakeholders;
>
> (c) The directors and officers played an integral role in identifying and facilitating potential transactions to explore during the SISP process;
>
> (d) The transactions approved by this Court resulted in the sale of substantially all of the Applicants' assets;
>
> (e) The transactions approved by this Court resulted in the preservation of a significant number of jobs both in Canada and the U.S.;
>
> (f) The releases will facilitate a monetary distribution of up to $1.5 million to the Applicants' major secured creditor, which funds would otherwise be held back for the charge to secure indemnity in favour of the directors and officers;
>
> (g) The key employee retention and incentive plan approved by this Court contemplated that the Applicants would seek a Court-ordered release of claims against the directors and officers;

(h) Creditors and stakeholders of the Applicants were put on notice of the Applicants' intention to apply for a release of claims against the directors and officers;

(i) The Applicants implemented enhanced notice provisions with respect to the release, which included mailing two letters to all known creditors of the Applicants as well as their current and former employees in both Canada and the U.S.;

(j) The releases will not affect claims against directors and officers that are covered by an applicable insurance policy of the Applicants;

(k) The releases are subject to limitations under section 5.1(2) of the CCAA, which provides for an exception to the release of claims that relate to contractual rights of creditors or are based on allegations of misrepresentations made by directors to creditors or of wrongful or oppressive conduct by directors;

(l) The releases would provide certainty and finality of the CCAA proceedings in the most efficient manner;

(m) A syndicate of lenders, as the Applicants' senior secured creditor, will suffer a substantial shortfall on the amounts owing to it, and as a result, a claims bar process and plan of arrangement would be cost-prohibitive;

(n) The CEO of the Applicants is not aware of any claim or proceeding in either Canada or the U.S. with respect to the directors or officers;

(o) The CEO is not aware of any party who has opposed or expressed an intention to oppose the releases and no one appeared at the hearing to oppose the releases;

(p) The Applicants' stakeholders had nearly two months to consider the terms of the release;

(q) Throughout the CCAA proceedings, the directors and officers acted in good faith and with due diligence; and

(r) The Monitor and agent in the present CCAA proceedings support the release.

Madam Justice Romaine prefaced her decision with the observation that the release of third party claims against directors and officers in a situation where there will not be a plan of arrangement is unusual, and that the relief with respect to the directors was granted in the specific circumstances of the case.[24] The Crown acknowledges the list of decisions cited by directors' counsel showing what Madam Justice Romaine described as unusual five years ago has since become the norm.

[24] *Entrec*, para. 2.

47. In his recent decision in *Delta 9 Cannabis Inc. (Re)*[25], Justice Marion cited the factors developed by the provincial superior courts relevant to those Courts' determinations of the propriety of releases:

> [62] Where releases are part of an RVO, then the factors noted above are also relevant (as adjusted for this context), namely:
>
> (a) whether the released claims are rationally connected to the purpose of the plan / transaction;
>
> (b) whether the plan / transaction can succeed without the releases;
>
> (c) whether the parties being released contributed to the plan / transaction;
>
> (d) whether the releases benefit the debtors as well as the creditors generally;
>
> (e) whether the creditors have knowledge of the nature and the effect of the releases; and
>
> (f) whether the releases are fair, reasonable and not overly broad.

48. The factors common to both Madam Justice Romaine's list and Justice Marion's list are the creditors' knowledge of the nature of the releases and the necessity of the releases for successful resolution of the corporate restructuring.

49. In the present case, the only known liability of the directors is their liability to the Minister for the *Excise Act, 2001* liability. Given the steps taken by the CRA before the CCAA proceeding and earlier this month, as authorized by Harris J, the directors can be assessed only for $4.7 million of Freedom's ~$9.7 million liability to the Minister under the *Excise Act, 2001* and not for any portion of their liability under the *Excise Tax Act* for Freedom's GST liability.

50. Under the common law test, the burden of proof is on the applicants to demonstrate on the balance of probabilities that the releases are appropriate in the circumstances, that they have been acting in good faith, and with due diligence.[26]

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[25] *Delta 9 Cannabis Inc (Re)*, 2025 ABKB 52 (CanLII).

[26] *Entrec*, *supra*, at para. 3, citing *9354-9186 Quebec Inc v Callidus Capital Corp*, 2020 SCC 10 at para 49.

51. Section 11 of the CCAA is introduced with the phrase, "Despite anything in the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*". It does not say "Despite any other enactment of Canada" or "Despite anything in the *Excise Act, 2001*". The Crown submits the propriety of an order made under section 11 should be made with consideration to all other law applicable to a given situation.

52. In *Baxter Student Housing Ltd. et al.* v. *College Housing Co-operative Ltd. et al.*, 1975 CanLII 164 (SCC), [1976] 2 SCR 475, the Supreme Court of Canada set aside the decision of the Manitoba Court of Queen's Bench declaring a receiver's charges had priority over a previously registered builders' lien claim. Dickson J (as he then was), writing for the Court, held the chambers justice's order was wrong in law because the priority order ran contrary to subsection 11(1) of *The Mechanics' Liens Act* of Manitoba prioritizing liens made under that Act. Justice Dickson went on to note:

> In my opinion the inherent jurisdiction of the Court of Queen's Bench is not such as to empower a judge of that Court to make an order negating the unambiguous expression of the legislative will. The effect of the order made in this case was to alter the statutory priorities which a court simply cannot do.
>
> In the Court of Appeal Matas J.A. per curiam said:
>
> > In any event, I am of the opinion that sec. 11(1), supra, cannot be interpreted, under the circumstances before us, so as to frustrate the jurisdiction of Court of Queen's Bench to appoint a receiver with effective power to carry out his mandate. (*Montreal Trust Company et al.* v. *Churchill Forest Industries (Manitoba) Limited,* 1971 CanLII 960 (MB CA), [1971] 4 W.W.R. 542 at p. 546 et seq.) In my view, the order appealed from is not in conflict with *The Mechanics' Liens Act*, *supra*, and is in accordance with its intent.
>
> *Montreal Trust Company et al.* v. *Churchill Forest Industries (Manitoba) Limited* may well be cited as a paradigm of the exercise of judicial discretion but Chief Justice Freedman, speaking for all his colleagues, was careful to state, p. 547:
>
> > Inherent jurisdiction cannot, of course, be exercised so as to conflict with a statute or Rule. Moreover, because it is a special and extraordinary power, it should be exercised only sparingly and in a clear case.

53. *Baxter Student Housing* considered the interplay between *The Court of Queen's Bench Act* of Manitoba (pursuant to which the receiver was appointed) and *The Mechanics' Lien Act* of Manitoba – two provincial statutes. The Supreme Court found the Court did not have

jurisdiction to make the impugned order in the receivership proceedings contrary to another provincial statute. In the present case, section 11 of the CCAA authorizes the Court to make any order it considers appropriate. The order sought is the release of the directors from their liability under another federal statute, the *Excise Act, 2001,* which, the company and the directors assert, is justified (a) because of their *ex post facto* contributions to the CCAA process, and (b) because is necessary for the future success of Freedom. As noted above, the *Excise Act, 2001* unambiguously prescribes a specific test, to be adjudicated before the Tax Court of Canada, to determine directors' liability. Under section 11, is it appropriate for the Court to substitute its own common law test to override the statutorily prescribed test?

54. The disconnect between the directors' liability provisions set out in the tax statutes and the common law tests formulated by the courts in restructuring proceedings is the different temporal foci of the tests. The tax statutes prescribe a review of the conduct of the directors at the time the tax debts arose, while the common law test focuses on the conduct of the directors in the restructuring process without any review of the directors' conduct giving rise to their liability. The jurisprudence interpreting the tax statutes specifically rejects evidence of what the directors did after the fact as a demonstration of due diligence at the relevant time – the very evidence the common law tests call for and that tendered by Mr. Potestio in this proceeding. The Crown has not found any decision that considers the tax statute decisions cited above in the context of director releases under the BIA or the CCAA.

55. Notably missing from the current formulation of the common law test are the considerations of the approval of the affected creditors (*Metcalfe* #6), and considerations of public policy (*Metcalfe* #7).

56. It is clear the affected creditor – the Crown – opposes the release of the directors. Because the directors have structured the CCAA proceedings to proceed by an RVO rather than putting a plan to their creditors, neither the Crown nor other affected creditors have the opportunity to express their approval or disapproval through a vote.

57. It equally clear that public policy – expressed in section 295 of the *Excise Act, 2001* – imposes liability on directors for their decisions at the expense of the public purse.

58. Moreover, as a matter of public policy, in order for law to be effective, breaches of the law must have consequences. The *Excise Act, 2001* imposes a legal obligation for licensees to

remit the prescribed taxes. Recognizing that directors are the directing minds and decision-makers of corporations, Parliament enacted s. 295 to incentivize directors to ensure the corporations under their control comply with those tax obligations. Releasing directors from statutory liability despite their complete failure to demonstrate the due diligence prescribed by law sends the message the Courts will not enforce the law enacted by Parliament and directors are free to ignore their statutory obligations without fear of consequence.

Purchaser's Condition Precedent not binding on the Court.

59. In the context of this (and similar) cases, the prospective purchaser includes a condition precedent in its offer that the directors must be released from liability. In the present case, Mr. Latimer has asserted that he wishes to retain the four individuals as directors of Freedom going forward. Their continued involvement, he asserts, is necessary for the post-closing viability of Freedom.

60. While the Stalking Horse Agreement provides that the Approval and Vesting Order must include a provision releasing (among others) the directors of Freedom from liability[27], the Court is not thereby bound to grant the releases. As noted by Koehnen J. in *Re. Green Relief Inc*. 2020 ONSC 6837 (CanLII), at paras. 13-15, characterization of the release as a condition precedent was irrelevant to his analysis and he considered himself free to approve the transaction with or without the release.

61. The overall purpose of Freedom's application is to continue in business by cleaning Freedom's balance sheet of the claims of its unsecured creditors while preserving both its tangible and intangible assets (i.e., licenses and tax losses).

62. Not releasing the directors from their statutory liability will not impede the execution of Freedom's "plan."

63. 2644323 Alberta Ltd. ("**264**"), a newly incorporated subsidiary of Freedom's senior secured creditor, JL Legacy Ltd., will become the sole shareholder of Freedom.

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[27] Affidavit of Johnfrank Potestio sworn February 18, 2025, Exhibit B (Stalking Horse Subscription Agreement) paragraph 1.1 (definition of "Approval and Vesting Order", subparagraph (v)(A)).

64. With the transfer of ownership, the directors of Freedom appointed by its previous shareholders are no longer necessarily going to be the shareholders of Freedom going forward. As the new owner / 100% shareholder of Freedom, 264 will have to appoint the directors of Freedom. There is a significant difference between the new owner *wanting* certain individuals as directors and the new owner *needing* those individuals to be directors.

65. Moreover, the ability of the four individuals to act as directors of Freedom going forward is not impaired if they are assessed under the *Excise Act, 2001*. Being assessed does not disqualify them from being directors. The rationale they express is that these individuals should spend their time focussed on the business of running the company rather than addressing their liability for their decisions , the same argument could be advanced in respect of any claim – civil or criminal. They argue they should be relieved of liability now so as not be distracted from their task of making money for their shareholder. The Crown submits this is not an appropriate rationale to release the directors from liability for their decisions.

All of which is respectfully submitted.

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