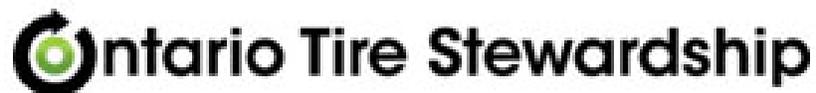


Ontario Tire Stewardship Wind Up Plan: Surplus Funds Addendum



Submitted to: Resource Productivity and Recovery Authority

Submitted on: January 12, 2021

Submitted by:

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Court Appointed Liquidator of Ontario Tire Stewardship

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Introduction: Ontario Tire Stewardship Wind Up Plan and Surplus Funds Direction

On March 16, 2020, the Ontario Superior Court of Justice (Commercial List) (the “**Court**”) issued an Order (“**Order Appointing Liquidator**”) that Ontario Tire Stewardship (“**OTS**”) be wound up pursuant to Section 243 of the *Corporations Act*, R.S.O. 1990, c. C. 38, as modified by Ontario Regulation 357/17. Grant Thornton Limited was appointed Liquidator (the “**Liquidator**”) of all of the assets, undertakings and properties of OTS for the purpose of winding up OTS’s business and affairs and distributing its property.

Paragraph 3 of the Order Appointing Liquidator states the “winding up shall be completed in accordance with the Corporation’s plan to wind up the Corporation, as prepared or amended pursuant to directions received from the Minister of the Environment, Conservation and Parks [(the “**Minister**”)], and as approved by the Resource Productivity and Recovery Authority (“**RPR**A”), including any conditions RPR A has determined or will determine are appropriate, or as otherwise ordered by the Court”.

On February 17, 2017, the Minister issued a letter directing the winding up of OTS in accordance with the provisions of the *Waste Diversion Transition Act*, 2016 and its regulations and also directed that OTS develop a plan which, among others, would provide a description and a proposal for the disposition of any program surpluses and deficits.

Subsequently, OTS conducted a consultation process in order to solicit the views from various industry participants regarding the wind up of OTS and the disposition of surplus funds. This consultation process led to the development of the OTS Wind Up Plan dated November 2017 (the “**WUP**”), which was then approved on March 22, 2018 by the RPR A Board following RPR A’s own consultation process.¹

Certain correspondence from the Minister was thereafter received by OTS where the Liquidator notes that on June 19, 2019, the Minister advised that due to uncertainty regarding the amount of surplus funds because of outstanding tax matters that are to be resolved, the Minister encouraged “OTS to design an amendment to the approved windup plan that will provide a high level of flexibility so that...as much of the surplus funds as possible [can be used] for the benefit of Ontario consumers”.

After the Liquidator’s appointment, the Minister issued a letter dated April 21, 2020 (the “**April 21st Direction**”) which directed OTS to amend its wind up plan. The key elements of the April 21st Direction include the following:

- Any remaining surplus funds are to be returned to stewards in proportion to the stewards’ contribution of the surplus in regard to tire classes that are in a surplus position;
- Stewards will use the surplus funds returned to them from OTS to offset fees they are currently paying to collect and manage tires under the producer responsibility framework;

¹ Under the Waste Diversion Transition Act, industry funding organizations such as Ontario Tire Stewardship are obligated to develop and submit wind up plans to RPR A in accordance with statutory requirements and the direction provided through the Minister’s direction. A copy of the approved wind up plan can be found here: <https://rpra.ca/wp-content/uploads/OTS-Wind-Up-Plan-1.pdf>

- Offsetting these costs is expected to benefit consumers when they purchase new tires;
- The deadline for OTS to submit the amended plan to RPRA for approval is within 10 weeks of receiving final ruling from the Canada Revenue Agency (“**CRA**”) on outstanding tax matters;
- It is the Minister’s expectation that the RPRA will approve amendments to the plan resulting from this clarification within 6 weeks of the plan being submitted by OTS; and
- Other than the clarification provided in the April 21st Direction, there are no changes to the requirements in previous direction letters.

This document, the OTS Wind Up Plan: Surplus Funds Addendum (the “**Addendum**”) outlines a proposal for a \$10 million interim distribution of surplus funds to stewards (the “**Proposal**”) consistent with the April 21st Direction. In developing this Proposal, the Liquidator also consulted key OTS stakeholder groups during the week of January 4, 2021. A list of stakeholder groups consulted, and a summary of their initial feedback is attached as an appendix to this Addendum.

With respect to other elements of the WUP, the Liquidator, in accordance with its statutory obligations, began implementing same upon its appointment.

Note: In preparing this Addendum, the Liquidator has relied upon certain audited and unaudited financial information, and other information contained in the books and records of OTS, as well as discussions with previous employees of OTS (collectively, the “**Information**”). The Liquidator has not audited, reviewed or otherwise attempted to verify the accuracy or completeness of the Information and the users are hereby cautioned.

Update on Outstanding HST Matters

Prior to the appointment of the Liquidator, there were certain outstanding input tax credits claimed by OTS which were being reviewed by Canada Revenue Agency (“**CRA**”). Related to this review, CRA conducted a review of the GST/HST returns of OTS for the months ended March 31, 2016 to December 31, 2018. On March 18, 2020, CRA issued a letter directly to OTS (the “**March 18th Letter**”), which was not received by the Liquidator until July 15, 2020.

The March 18th Letter proposed adjustments which indicated that an HST liability of \$19.5 million (the “**HST Liability**”) was owed. The proposed adjustments were based on a decision from the Tax Court of Canada (“**TCC**”) dated March 21, 2018 which involved Stewardship Ontario, where the CRA is now taking the position that OTS should have been collecting and remitting tax on the Tire Stewardship Fee (“**TSF**”), as TSF was considered a taxable supply in the Stewardship Ontario case. Prior to this decision of the TCC, OTS was not invoicing the stewards and charging HST on the TSF, as the Liquidator understands that CRA had accepted such practice at that time, as OTS was complying with the October 28, 2013 GST/HST ruling – Stewardship fees Paid to Industry Funding Organizations.

The Liquidator understands that CRA intends to issue to OTS a formal notice of assessment for the HST Liability and any adjustments thereto. Until a notice of assessment is received and until the Liquidator carefully reviews the notice of assessment, the Liquidator is not making any further comment or

recommendation in this Addendum regarding this matter, as resolution of the HST Liability does not impact the Proposal.

Tire Classes Eligible to Share in the Surplus

The April 21st Direction stated, among others, that “[a]ny remaining surplus funds are returned to stewards in proportion to the stewards’ contribution of the surplus in regard to tire classes that are in a surplus position”. Since being formed in 2009, OTS recorded TSF revenue on a class by class basis. OTS advised the Liquidator that during the years 2009 to mid-2013, there were only 8 classes of tires: Class 1 – Passenger Light Tires (“**PLT**”); Class 2 – Medium Truck (“**MT**”); and Classes 3 to 8 – Off the Road (“**OTR**”). From mid-2013 to 2018, the OTR category was expanded from 6 classes to 16 classes. Expenses related to Collection Allowances, Transportation Incentives, Processing Incentives, and Manufacturing Incentives, were recorded by OTS only under the three tire categories (PLT, MT and OTR) (the “**Three Tire Categories**”). OTS allocated expenses specific to each type of incentive based on weighted averages or on Hauler Volume Reports which tracked tire weights among the Three Tire Categories.

The Liquidator obtained the financial results of each of the Three Tire Classes since OTS’ date of inception to the date its normal operations ceased, that being December 31, 2018. The Liquidator believes the first step is to determine which tire classes are in a surplus or deficit position. The Liquidator has summarized this information in Table 1 below²:

Table 1		OTS - Excess Revenue Over Expenses - Surplus/(Deficit)			
Year	PLT (Class 1)	MT (Class 2)	OTR (Class 3-18)	Net	
2009	8,156,147	(1,616,241)	(2,162,185)	4,377,721	
2010	14,646,014	(1,915,117)	(7,064,560)	5,666,337	
2011	14,127,256	(3,382,558)	(6,446,456)	4,298,242	
2012	12,509,937	(3,597,326)	(5,810,154)	3,102,457	
2013	15,175,472	(2,597,648)	(1,326,737)	11,251,087	
2014	19,808,140	(821,481)	1,417,064	20,403,723	
2015	12,122,490	(2,010,173)	2,612,315	12,724,632	
2016	(7,129,110)	(5,907,175)	367,297	(12,668,988)	
2017	(7,210,363)	(6,013,602)	3,166,265	(10,057,700)	
2018	465,458	1,827,682	7,450,572	9,743,712	
2019	(4,104,906)	-	-	(4,104,906)	
2020	-	-	-	-	
Total	78,566,535	(26,033,639)	(7,796,579)	44,736,317	

In light of the foregoing, allocation of the annual surplus’ and deficits to each of classes 3 to 18 is not feasible and allocation can only be completed for OTR as a whole. Accordingly, the Liquidator believes that the table above represents the best and only reasonable depiction of the annual surplus’ and deficits for each of the Three Tire Categories.

² Notes on financial results included in the table: i) The net column agrees to the OTS audited financial statements for each of the respective years. ii) The allocation among the classes for the period 2009 to 2013 was obtained from the “Report on Specified Auditing Procedures” dated March 19, 2015 prepared by KPMG LLP. iii) The allocation among the classes for the period 2014 to 2018 was obtained from the OTS Management Reports which were all validated by OTS except for calendar year 2018. iv) The final amount of the surplus available for distribution will not be known for such matters as: (a) outstanding tax matters are resolved; (b) financial results for the period January 1 to March 16, 2020 are finalized; and (c) the costs incurred during the liquidation proceedings are considered.

In interpreting the April 21st Direction, the first determination is which tire classes (i.e. the Three Tire Categories) are in a surplus position. The Liquidator believes this part of the April 21st Direction to mean the cumulative surplus or deficit (i.e. as at December 31, 2018) is the determining factor.

Based on the Liquidator's review of the books and records of OTS, reliance on the audited financial statements from KPMG, reliance on the specified auditing procedures report prepared by KPMG, reliance on the OTS Management Reports, and the allocation assumptions which are summarized in the table above, only PLT – Class 1 is in a surplus position. Therefore, the Liquidator suggests that only those stewards in PLT – Class 1 are eligible to share in the surplus after deducting incurred and future expenses related to the liquidation proceedings from the net funds on hand. The Liquidator further suggests that the April 21st Direction does not specify that the cumulative deficits in MT and OTR “be made whole” by the stewards in those two tire categories; this supports the notion of the PLT – Class 1 stewards sharing in only the net funds on hand.

Proposed Surplus Allocation Methodology and Proposal

The Liquidator is proposing the following methodology in determining the allocation of surplus to the stewards in PLT – Class 1:

1. OTS tracked the number of tires supplied by stewards by each of the 18 classes of tires and manually adjusted same to only reflect those that were supplied to Ontario. The tires supplied in each class of tires were then converted to an industry standard measurement, that being Passenger Tire Equivalent (“PTE”).
2. For PLT – Class 1, the Liquidator reviewed all of the data provided by OTS relating to PTE for each of the years 2009 to 2018. The stewards who represented approximately 90% of the PTE in each of those years were generally the same, and whose rankings in terms of sales did not materially change year to year. However, there were a number of stewards outside of the top 90% whose supplied amounts differed.
3. The Liquidator considered various methodologies to allocate surplus to the stewards in PLT – Class 1 and proposes to make an interim distribution to the stewards so entitled once the notice of assessment from CRA has been received and requisite approvals are received.
4. The Liquidator would allocate each year's net surplus or deficit (i.e. the right hand column of Table 1) to each steward in PLT – Class 1 based on their proportion of PTE supplied each year.
5. The Liquidator would then sum the allocations for each year for each steward (i.e. as determined in step 4), which then represents each steward's share of the net excess revenue over expenses for the period 2009 to 2018 of \$48,841,223 (the “**Total Allocation**”). The deficit in 2019 of \$4,104,906 represents costs which would be allocated on the basis of each steward's proportion of the Total Allocation.
6. Under the assumption that the notice of assessment does not materially differ from the HST Liability, the Liquidator's Proposal is to recommend an interim distribution of \$10 million to the stewards in PLT – Class 1, which the Liquidator considers appropriate given resolution to the HST Liability will take some time and taking into account claims and future expenses related to the liquidation proceedings.

7. The Liquidator would allocate the proposed \$10 million interim distribution to such stewards based on each steward's proportion of the Total Allocation and facilitate the \$10 million interim distribution. More specifically, the \$10 million interim distribution is determined as follows:

	CY2020	CY2021	CY2022
	Actual	Estimate	Estimate
CASH RECEIPTS			
Cash Received by Liquidator (Note 1)	\$ 42,382,486	\$ -	\$ -
Various Refunds and Sundry Receipts	70,629	-	-
	\$ 42,453,114	\$ -	\$ -
CASH DISBURSEMENTS			
RPRAs Fees to October 31, 2020 (Note 2)	\$ 621,896	\$ 960,000	\$ 480,000
Legal Fees to November 30, 2020 (Note 2)	222,744	260,000	160,000
Liquidator's Fees to November 30, 2020 (Note 2)	157,981	500,000	180,000
Computer Services and Licence Fee	96,492	530,000	80,000
HST on Cash Disbursements	118,929	296,400	120,900
Outside Consulting	11,411	20,000	20,000
Storage and Utilities	3,564	10,000	10,000
HST Assessed Liability	-	19,492,160	-
Contingency (Note 3)	-	2,000,000	6,100,637
	\$ 1,233,017	\$ 24,068,560	\$ 7,151,537
RECEIPTS LESS DISBURSEMENTS	\$ 41,220,097	\$ (24,068,560)	\$ (7,151,537)
SURPLUS FUNDS AVAILABLE FOR INTERIM DISTRIBUTION			\$ 10,000,000

NOTES

Note 1: The net cash balance received by the Liquidator is calculated as follows:

Surplus revenue from 2009 to 2018	\$ 48,841,223
Less: deficit incurred in 2019	(4,104,906)
Less: accrual for future potential input tax credits	(2,353,831)
	\$ 42,382,486

Note that the above CY2020 cash receipts and disbursements include activity from the date of the Liquidator's appointment on March 16, 2020. Full disclosure of the 2020 financial results, including CY2020 financial activity prior to the date of liquidation, will be reflected in the OTS Annual Report which will be released in April 2021.

Note 2: As at December 31, 2020, the RPRAs fees for the months of November and December have not been paid but are included in CY2021 estimates, the amounts of which are not expected to be materially different than the current run rate. Liquidator fees and fees of its legal counsel for the month of December have not been not been paid as at December 31, 2020 and have been included in CY2021 estimates.

Note 3: The Liquidator included a provision for tax liabilities owing until such time that the notice of assessment is received from CRA and after a final audit on all tax matters is performed by CRA. In addition, the Liquidator established a provision for potential claims.

8. Due to the costs of preparing and issuing payments, tracking and related banking matters thereof, the Liquidator proposes that no distributions be made to those stewards who have their proportion

of the Interim Distribution less than \$250. The Liquidator would redistribute the surplus from stewards below this threshold proportionately to the remaining stewards.

9. A further interim distribution may occur, or the Liquidator may elect to issue a final distribution, depending on the status of resolving the HST Liability, subject to a future consultation process, and receiving requisite approvals from RPRA and the Court.

Use of Funds to Benefit Consumers

As previously mentioned, the April 21st Direction stated “[t]ire stewards will use the surplus funds returned to them from OTS to offset fees they are currently paying to collect and manage tires under the producer responsibility framework...Offsetting these costs is expected to benefit consumers when they purchase new tires” (the “**Minister’s Consumer Direction**”).

Considering the alternatives from cost efficient and program effectiveness perspectives as well as recognizing the varying circumstances of each and every steward, the Liquidator suggests that at a minimum, each steward receive a letter (the “**Acknowledgement Letter**”) which would accompany the payment of their share of the \$10 million interim distribution. This Acknowledgement Letter would advise, among others, that by accepting and depositing this interim distribution of surplus, the steward acknowledges the Minister’s Consumer Direction and will use its best efforts to follow the spirit and intention of same.³

The Liquidator proposes that in regard to the \$10 million interim distribution, it will provide interim reports to RPRA on a quarterly basis detailing the amount of funds disbursed to OTS stewards, and the number of stewards who have accepted the funds, thereby acknowledging the Minister’s Consumer Direction. Additionally, the Liquidator proposes to provide RPRA with interim reports on the number of stewards that refuse to accept the funds and who do not acknowledge the Minister’s Consumer Direction per the Acknowledgement Letter. In circumstances, where stewards are unable to adhere to the Minister’s Consumer Direction or who are unresponsive, the Liquidator will seek court approval in order to put such funds back into the pool and reallocate and disburse those funds to those stewards who have acknowledged the Minister’s Consumer Direction.

Conclusion

The Liquidator suggests that it make a \$10 million interim distribution to stewards so entitled, recognizing that it will take time to resolve the HST Liability.

It is the view of the Liquidator that the Proposal contained herein is consistent with the April 21st Direction. In summary, the Liquidator believes that only stewards in PLT – Class 1 should receive their pro-rata share in the \$10 million interim distribution, as careful review of historical information indicates that this is the only tire class in a surplus position.

³ The Acknowledgement Letter issued to stewards would include the following sample language: “By accepting the enclosed interim distribution cheque, you understand the terms contained herein and acknowledge the expectation of the Minister of Environment, Conservation and Parks that the enclosed distribution cheque will be used for the benefit of Ontario consumers.”

While alternate surplus sharing calculation methodologies were considered with respect to this Proposal (to include collecting stewards' share of deficits in the classes of tires other than PLT – Class 1), in the view of the Liquidator, the higher administrative costs associated with such methodologies are not warranted (and where ultimate success is not guaranteed and, as the Liquidator submits, is not achievable) and would negatively affect the net distribution to be received by stewards, and ultimately the end consumer.

The Liquidator believes an Acknowledgment Letter confirming each steward's understanding of the \$10 million interim distribution will adhere to the April 21st Direction, based on its discussions with stakeholders during the Liquidator's consultation process. Moreover, this method provides flexibility for stewards to develop and implement their own method of benefiting the Ontario consumer on the purchase of new tires, depending on each steward's own unique circumstances.

The Liquidator believes that this Addendum and the process to develop the such amendments to the WUP meet the requirements of the Minister's direction, the WDTA and the Guiding Principles as outlined in RPRA's Wind-up Guide. The Liquidator believes that the Proposal set forth is fair and equitable and that the plan is cost effective and efficient.

Appendix: Consultation Meetings on Distribution of Surplus Funds

The Liquidator contacted the three principal associations and six of the largest stewards in terms of the supply of tires. The Liquidator then reviewed a draft of its recommendations regarding the \$10 million interim distribution and methodology with two associations and five stewards during the week of January 4, 2021. The Liquidator expects to have similar discussions with remaining association and steward in the coming days.

The organizations which provided initial feedback on the Liquidator's proposals included the following:

- Ontario Tire Dealers Association
- Tire and Rubber Association of Canada
- Michelin North America (Canada) Inc.
- Canadian Tire Corporation Limited
- FCA Canada Inc.
- Ford Motor Company of Canada Limited
- General Motors of Canada Company

It should be noted that given the timeframes associated with the consultation, the summary of initial feedback referenced below may not reflect the full views of any of the above organizations in relation to the proposed interim distribution of \$10 million.

The proposal regarding the \$10 million interim distribution was sent to these participants in advance of consultations, in the form of a slide deck highlighting the key elements of the distribution methodology, the proposed allocation of surplus funds, and the proposed interim distribution of \$10 million. Additionally, during the consultations, discussions ensued with respect to funds being used for the benefit of the end consumer. It is noted that while the HST Liability was discussed on a preliminary basis during the consultations, the discussion with respect to the Liquidator's final resolution of same was not discussed, as the notice of assessment has not been received from CRA and, therefore, the Liquidator was not in a position to provide a final and complete analysis of same.

The following is a summary of the key points that were raised by stakeholders during the consultation meetings:

- Certain participants questioned the appropriateness of subsidizing deficits in the MT and OTR classes when they only supplied tires under PLT – Class 1. The Liquidator explained that the April 21st Direction states that “[a]ny remaining surplus funds are returned to stewards in proportion to the stewards’ contribution of the surplus in regard to tire classes that are in a surplus position.” After review of PLT, OTR and MT’s proportionate share of net revenue from 2009 to 2018, it is evident that PLT was the only class in a surplus position. Therefore, while the Liquidator understands the concern put forth, the Liquidator believes that its Proposal is in conformance with

the April 21st Direction. The Participants understood the complexity of this issue, and agreed that a simpler approach may be beneficial for the majority of stewards.

- Stakeholders questioned how surplus funds should be used to benefit the end consumer and were concerned that it would be difficult to retroactively apply the surplus funds received to past consumers. The Liquidator’s interpretation of the April 21st Direction is that the interim distribution of \$10 million received by stewards should benefit consumers on the future purchase of new tires. Participants understood that an acknowledgement would accompany the interim distribution received and it would be to their discretion on how to apply the benefit to consumers.
- With respect to reimbursing consumers on the future purchase of new tires, one concern was how this would affect a steward’s periodic third party audits on fees being paid by a steward to a Producer Responsibility Organizations (“**PROs**”). If a steward chose to apply the surplus as a reduction in future tire levies to end consumers, the question arose as to how this would then reconcile in a third party audit engaged by a PRO. In this scenario, and while each individual steward will handle the consumer reimbursement differently, it was discussed that a steward may be responsible to provide notice to the PRO regarding the steward’s policy.

With respect to the main elements of the allocation of the surplus and methodology for the \$10 million interim distribution, stakeholders voiced support for the proposed methodology described above. As such there were no objections to restricting surplus fund payments to stewards in the PLT – Class 1 category. The amount of the \$10 million interim distribution was agreed upon by all stakeholders. Additionally, stakeholders agreed that an acknowledgement letter to confirm each steward’s understanding of the use of funds for the benefit of the end consumer is a reasonable approach and would likely be accepted by the stewards in general.