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• KEY AMENDMENTS TO THE *BIA* AND *CCAA* — HOW WILL THEY CHANGE RESTRUCTURING PRACTICE IN CANADA? •

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I. INTRODUCTION

In connection with the amendments made to the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (“*BIA*”) and the *Companies’ Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (“*CCAA*”) in 1997, statutory provisions were included requiring that the administration and operation of the *BIA* and the *CCAA* be reviewed by parliamentary committees within five years. As a result, the past decade has seen considerable review of the provisions of bank-

ruptcy and insolvency law in Canada in an effort to determine whether such laws were meeting the needs of debtors, creditors and insolvency professionals, among others. The culmination of such review was the passage of two statutes that significantly amend the *BIA* and the *CCAA*, namely the *Wage Earner Protection Program Act*, S.C. 2005, c. 47 (“Chapter 47”) and further amendments passed in 2007 (S.C. 2007, c. 36) (“Chapter 36”). The amendments to the *BIA* and the *CCAA* contained in Chapter 47 and Chapter 36 have now been proclaimed into force. This article considers the amendments to the *BIA* and the *CCAA*, and the effect, if any, that such amendments will have on insolvency practice in the following topic areas:

- Contract Rejection;
- Asset Sales;
- DIP financing;
- Remedies;
- Restructuring with existing collective agreements;
- New receivership provisions;
- Treatment of equity claims; and
- Protection of Professionals.

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II. CONTRACT REJECTION

The *BIA* and *CCAA* in their previous forms did not specifically address the ability of a debtor, trustee or receiver to disclaim or assign agreements, other than with respect to leases, in the case of a bankruptcy or proposal proceeding. With the new amendments to the *BIA* and *CCAA*, the courts are now able to rely on specific provisions of each act in order to approve the disclaimer or assignment of an agreement in proceedings commenced under either the *BIA* or *CCAA*.

A. *BIA**DISCLAIMER OF AGREEMENTS: SECTION 65.11*

Amendments to the *BIA* now enable a debtor to disclaim and resiliate agreements besides leases. In accordance with the “new” s. 65.11, a debtor who has filed a notice of intention to make a proposal (“NOI”) or a proposal, now has the express authority, subject to receiving approval by the trustee or alternatively the court, and on notice to the other parties to the agreement and the trustee, to disclaim or resiliate any agreement to which they are a party on the day of filing of the NOI or proposal, aside from those set out in subs. (10).

When considering whether or not to make such an order, the court is to consider the following factors:

- (a) whether the trustee approved the proposed disclaimer or resiliation;
- (b) whether a termination or repudiation would make the proposal more viable; and
- (c) whether the counterparty would suffer substantial financial hardship as a result of the termination or repudiation.

Pursuant to subs. 65.11(3), a party to the agreement may, within fifteen days of receiving the notice of disclaimer from the debtor, appeal the disclaimer. Pursuant to subs. 65.11(8), a party who suffers a loss from a successfully disclaimed agreement will have a provable claim in the proposal.

Pursuant to subs. 65.11(7) if a debtor has granted a party a right to use intellectual property, a disclaimer or resiliation under this section does not affect that party’s right to use the intellectual property, including the party’s right to enforce its exclusive use, so long as the party continues to perform its obligations under the agreement in relation to the use of the intellectual property.

Pursuant to subs. 65.11(10), a debtor's ability to disclaim an agreement does not extend to the disclaimer of:

- (a) eligible financial contracts;
- (b) a lease referred to in subs. 65.2(1);
- (c) a collective agreement;
- (d) a financing agreement if the debtor is the borrower; or
- (e) a lease of real property or of an immovable if the debtor is the lessor. Eligible financial contracts have been redefined under the amendments by the broader definition of "an agreement of a prescribed kind."

The amendments to the *BIA* do not include a similar provision for bankruptcies or receiverships and accordingly trustees and receivers will need to continue to rely on the established right to disclaim an agreement under the common law in the context of such proceedings.

ASSIGNMENT OF AGREEMENTS: SECTION 84.1

Subject to any anti-assignment provisions contained in an agreement, trustees previously utilized subs. 30(1)(a) of the *BIA* (which gives a trustee the general power to sell or otherwise dispose of all or part of the debtor's property), to assign an agreement in a bankruptcy context. Section 84.1 as enacted has given trustees the express statutory right to assign an agreement to a third party, subject to approval by the court. In determining whether or not to grant the order (subs. 84.1(4)) the court must consider whether the person to whom the rights and obligations are to be assigned is able to perform the obligations and whether it is appropriate to assign the rights and obligations to that person. Pursuant to subs. 84.1(5), the court must also be satisfied that all monetary defaults under the agreement will be remedied on or before the proposed date of assignment. The ability to assign agreements granted by s. 84.1 is also now available in the context of an NOI or a proposal pursuant to s. 66(1.1) of the *BIA*. Eligible financial contracts and collective agreements are exempted from the assignment provisions under ss. 84.1 and 66(1.1).

DISCLAIMER AND ASSIGNMENT OF LEASES

Under s. 30(1)(k) a trustee was previously able to assign or disclaim a real property lease in conjunction

with ss. 38 and 39 of the *Commercial Tenancies Act (Ontario)*, R.S.O. 1990, c. L. 7. Similarly, pursuant to s. 65.2 of the *BIA*, a tenant was previously able to disclaim a lease in a proposal proceeding. Under the new amendments to the *BIA* the assignment of leases in bankruptcy and proposal contexts is now governed by ss. 84.1 and 66(1.1) respectively, however the disclaimer of leases remains subject to existing ss. 30(1)(k) and 65.2 of the *BIA*.

TERMINATION OF AGREEMENTS: SECTION 65.1 AND SECTION 84.2

The protection historically afforded to a debtor who had filed an NOI or a proposal against the termination or amendment of an agreement on the basis of the filing of the proposal pursuant to s. 65.1 of the *BIA* has been extended by the amendments to apply to bankrupts as well with the addition of s. 84.2. Section 84.2, however, does not protect against the termination or amendment of eligible financial contracts, which are exempt from the rule.

Section 65.1 has also been expanded by the amendments to protect agreements, including security agreements, from termination or amendment by reason only of the debtor filing an NOI or proposal. Again, eligible financial contracts are excluded from the application of this section.

B. CCAA

DISCLAIMER OF AGREEMENTS: SECTION 32

Prior to the enactment of s. 32 of the *CCAA*, which mirrors s. 65.11 of the *BIA*, the courts in *CCAA* proceedings were only able to authorize the disclaimer of an agreement by way of s. 11 of the *CCAA* and the discretionary powers granted to the court thereunder. Section 32 now grants to a debtor company the same express authority to terminate and resiliate agreements as is granted to debtors under s. 65.11 of the *BIA*. Under s. 32 the monitor acts as the gatekeeper rather than the trustee.

ASSIGNMENT OF AGREEMENTS: SECTION 11.3

Section 11.3 of the *CCAA* has been amended to mirror the s. 84.1 of the *BIA* and grant a debtor the express authority to assign an agreement. The factors to be considered by the court are virtually identical to

those found in s. 84.1 of the *BIA*, with the addition of one further; the court must consider whether the monitor approves of the proposed assignment. As in s. 84.1, all monetary defaults must be remedied.

DISCLAIMER AND ASSIGNMENT OF LEASES: SECTION 32 AND 11.3

Although the *BIA* contains specific provisions for disclaiming or assigning leases, the right to do so under the *CCAA* is now governed by the general disclaimer and assignment provisions of ss. 32 and 11.3.

III. ASSET SALES

The *BIA* and the *CCAA* in their previous forms did not specifically address the ability of a debtor in a *BIA* proposal proceeding or a *CCAA* proceeding to sell all or a portion of its business and/or property in order to, among other things, generate capital necessary to implement a proposal or plan of compromise or arrangement. Notwithstanding this, Ontario courts had held that the court, through its inherent jurisdiction to fill in gaps in legislation, could grant orders for the sale of substantially all of the assets of the debtor company prior to a proposal or a plan of compromise or arrangement being in place before the creditors for consideration. This reality was reflected in paragraph 11(e) of the standard form template initial *CCAA* order approved by the Commercial List Users' Committee (the "**Model Initial CCAA Order**"), which grants the debtor company the right to pursue offers for material parts of its business or property, in whole or part, subject to prior approval of the court being obtained before any sale.

Pursuant to the enactment of Chapter 47 and Chapter 36, the *BIA* and the *CCAA* have been amended to include specific provisions dealing with the ability of a debtor to sell its assets outside of the ordinary course of business with court approval during restructuring proceedings.

A. *BIA* AND *CCAA*

RESTRICTION ON SALE OF ASSETS

Section 65.13(1) of the *BIA* and s.36(1) of the *CCAA* provide that an insolvent person/debtor company may not sell or otherwise dispose of assets outside the ordinary course of business unless it is

authorized to do so by a court. The sections also provide that, despite any requirement for shareholder approval, including under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained. In the case of proposals under the *BIA* where the insolvent person is an individual carrying on a business, Section 65.13(2) provides that the court may authorize the sale or disposition only if the assets were acquired for or used in relation to the business.

NOTICE TO SECURED CREDITORS

Section 65.13(3) of the *BIA* and s.36(2) of the *CCAA* provide that the insolvent person/debtor company applying to the court for authorization to sell or otherwise dispose of its assets outside the ordinary course of business is required to give notice of the application to the secured creditors who are likely to be affected by the proposed sale or disposition.

FACTORS TO BE CONSIDERED BY THE COURT

Section 65.13(4) of the *BIA* and s.36(3) of the *CCAA* provide a list of non-exhaustive factors that a court is to consider in deciding whether to grant the authorization for the sale or disposition. The enumerated factors are:

- (a) whether the process leading to the proposed sale or disposition was reasonable in the circumstances;
- (b) whether the trustee/monitor approved the process leading to the proposed sale or disposition;
- (c) whether the trustee/monitor filed with the court a report stating that in their opinion the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy;
- (d) the extent to which the creditors were consulted;
- (e) the effects of the proposed sale or disposition on the creditors and other interested parties; and
- (f) whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.

RELATED PERSONS

Section 65.13(5) of the *BIA* and s.36(4) of the *CCAA* provide that, where the proposed sale or disposition is to a person who is "related" to the insolvent per-

son/debtor company, the court may, after considering the factors reproduced above, grant the authorization only if it is satisfied that good faith efforts were made to sell or otherwise dispose of the assets to persons who are not related to the insolvent person/debtor company, and the consideration to be received is superior to the consideration that would be received under any other offer made in accordance with the process leading to the proposed sale or disposition. For the purposes of the sections, a person who is related to the insolvent person/debtor company includes:

- (a) a director or officer of the insolvent person/debtor company;
- (b) a person who has or has had, directly or indirectly, control in fact of the insolvent person/debtor company; and
- (c) a person who is related to a person described in (a) or (b) (s. 65.13(6) of the *BIA* and s. 36(5) of the *CCAA*).

ASSETS MAY BE DISPOSED FREE AND CLEAR

Section 65.13(7) of the *BIA* and s. 36(6) of the *CCAA* now provide that the court may authorize a sale or disposition free and clear of any security, charge, or other restriction and, if it does, it shall also order that other assets of the insolvent person/debtor company or the proceeds of the sale or disposition be subject to a security, charge or other restriction in favour of the creditor whose security, charge or other restriction is to be affected by the order.

EMPLOYER RESTRICTIONS

Section 65.13(8) of the *BIA* and s.36(7) of the *CCAA* now provide that the court may only grant the authorization if it is satisfied that the insolvent person/debtor company can and will make the payments that would have been required for unpaid wages and unpaid pension plan contributions if the court had sanctioned the proposal/plan of compromise or arrangement.

EFFECTS OF AMENDMENTS ON RESTRUCTURING PRACTICE

The amendments made to the *BIA* and the *CCAA* with respect to asset sales largely codify existing practice and are substantially based on the recommendations made by insolvency professionals. By codifying

existing practice, the *BIA* and the *CCAA* now provide express jurisdiction to the courts to authorize the sale of assets and greater certainty and clearer direction to the parties involved in the asset sale process, be it the debtor, a proposed purchaser or the court. The amendments to the *BIA* and the *CCAA* do not specifically address the methods by which the sale process may be conducted (i.e. by auction or by “stalking horse” bid process) and any issues that may arise in connection with the sale process (such as the payment of “break fees” to the stalking horse). However, the interested parties can address these issues at the time when the court establishes the sales process or the court is considering whether to authorize and approve the transaction.

IV. DIP FINANCING

The *BIA* and the *CCAA* in their previous forms did not specifically address the ability of a debtor in a *BIA* proposal proceeding or a *CCAA* proceeding to obtain interim financing, or debtor-in-possession (“**DIP**”) financing, in order to continue operating during its restructuring proceeding, or the ability of a court to grant a super-priority charge over the property, assets and undertaking of the debtor in an effort to protect the DIP lender and permit the DIP lender to be repaid in priority to the other secured creditors of the debtor. As a result, courts typically had to rely on their inherent jurisdiction to authorize debtors to enter into DIP financing arrangements and to grant super-priority charges to DIP lenders. Paragraphs 32-37 of the Model Initial *CCAA* Order reflects this reality by, *inter alia*, authorizing the debtor to obtain DIP financing to finance its working capital requirements, and granting the DIP lender a super-priority charge.

Following the enactment of Chapter 47 and Chapter 36, the *BIA* and the *CCAA* have been amended to include specific provisions dealing with the ability of a debtor to obtain DIP financing to fund its working capital requirements during its restructuring proceeding, and the ability of the court to grant a super-priority charge to the DIP lender.

A. *BIA* AND *CCAA*

APPLICATION AND NOTICE

Section 50.6(1) of the *BIA* and s. 11.2(1) of the *CCAA* provide that the debtor in the *BIA* proposal or

CCAA proceedings is to bring an application for approval of interim financing by the Court. The application is to be on notice to the secured creditors who are likely to be affected by any security or charge that the Court may grant in connection with the interim financing. In the case of a *BIA* proposal proceeding commenced by an individual, s. 50.6(2) of the *BIA* provides that the individual cannot make an application unless they are carrying on a business.

INTERIM FINANCING ORDER

Section 50.6(1) of the *BIA* and s.11.2(1) of the *CCAA* provide that the Court may make an order declaring that all or part of the debtor's property is subject to a security or charge, in an amount that the court considers appropriate, in favour of a person specified in the order who agrees to lend to the debtor an amount approved by the court as being required by the debtor, having regard to the debtor's cash-flow statement. The security or charge may not secure an obligation that exists before the order is made. In the case of a *BIA* proposal proceeding commenced by an individual, s. 50.6(2) of the *BIA* provides that only the property acquired by or used in relation to the business may be subject to a security or charge.

PRIORITY OF CHARGE

Section 50.6(3) of the *BIA* and s. 11.2(2) of the *CCAA* provide that the court may order that the security or charge rank in priority over the claim of any secured creditor of the debtor. Where a court has previously granted an interim financing order, s. 50.6(4) of the *BIA* and s. 11.2(3) of the *CCAA* provide that the court may order that a new interim financing security or charge ranks in priority over the security or charge granted in connection with a previous interim financing order only with the consent of the person in whose favour the previous order was made.

FACTORS TO BE CONSIDERED

Section 50.6(5) of the *BIA* and s. 11.2(4) of the *CCAA* provide a non-exhaustive list of factors that the court is to consider in deciding whether to make an interim financing order. The enumerated factors are:

(a) the period during which the debtor is expected to be subject to proceedings;

- (b) how the debtor's business and financial affairs are to be managed during the proceedings;
- (c) whether the debtor's management has the confidence of its major creditors;
- (d) whether the loan would enhance the prospects of a viable proposal/plan of compromise or arrangement being made in respect of the debtor;
- (e) the nature and value of the debtor's property;
- (f) whether any creditor would be materially prejudiced as a result of the security or charge; and
- (g) the monitor's/trustee's report to the court on the cash-flow statement of the debtor.

EFFECT OF AMENDMENTS ON RESTRUCTURING PRACTICE

The amendments to the *BIA* and the *CCAA* with respect to interim or DIP financing have largely codified the court's power to authorize DIP financing and provide statutory guidance to the courts with respect to the factors to be considered prior to granting such financing.

V. REMEDIES

A. *BIA*

The remedies section of the *BIA*, previously ss. 91 through to 101 and entitled "Settlements and Preferences" was significantly overhauled by the amendments. The section was renamed "Preferences and Transfers at Undervalue" and has repealed ss. 91 and 100 and wholly replaced ss. 95 and 96. The new section focuses on scrutinizing transfers made at undervalue (as the new name would suggest) and imports an effects-based test for non-arm's-length transfers, as well as longer look-back periods for all questionable transactions.

The preliminary considerations of whether the transfer was at undervalue and whether the parties were at arm's length or not are questions of fact to be determined by the court. Section 2 of the *BIA* now includes a definition for "transfer at undervalue", describing the same as:

a disposition of property or provision of services for which no consideration is received by the debtor or for which the consideration received by the debtor is

conspicuously less than the fair market value of the consideration given by the debtor.

With respect to the determination of whether parties are at arm's-length or not, the newly created s. 4(5) of the *BIA* makes the presumption that persons who are related to each other are deemed not to deal with each other at arm's length while so related, and that for the purpose of ss. 95 and 96, in absence of evidence to the contrary, persons are deemed *not* to deal with each other at arm's length.

SECTION 95

Subsection 95(1) did not previously discern whether the creditor was arm's length or not. It required only that the transferor be insolvent at the time of transfer and that the transfer be made with a view to prefer within three months of the initial bankruptcy event in order to deem a transfer fraudulent and void. The amendments have expanded subs. 95(1) to contemplate transfers made to non-arm's length parties and broadened review powers with respect to such transfers.

Under the "new" subs. 95(1), the same requirements exist for arm's-length transfers; a transfer by an insolvent person with a view to preferring in the three months prior to the initial bankruptcy event. Under the "new" subs. 95(1) however, the ability to review non-arm's length transfers has been broadened. The requirement to prove intent has been removed from the test and as between non-arm's-length parties it is no longer necessary to show that the transfer was made with a view to prefer, only that the transfer had the effect of preferring.

SECTION 96

The amended s. 96 has also broadened the scope for attacking transactions at undervalue and extends the potential look-back periods for such "transactions at undervalue". On application by the trustee, the court may declare a transfer at undervalue to be void as against the trustee, or order a party to the transfer or any other person who is privy to the transfer, to pay to the estate the difference between the value of consideration received by the debtor and the value of the consideration given by the debtor.

Under subs. 96(1), in order for a transfer between *arm's length* parties to be subject to attack, the trustee must establish:

1. that the transfer was at undervalue;
2. that the transfer occurred within a year of the date of the initial bankruptcy event;
3. that the debtor was insolvent at the time of the transfer or was rendered insolvent by it; and
4. that the debtor intended to defraud, defeat or delay a creditor.

Under subs. 96(1), in order for a transfer between *non-arm's-length* parties to be subject to attack, the trustee need only establish:

1. that the transfer was at undervalue; and
2. that the transfer occurred within a year of the date of the initial bankruptcy event.

If the trustee is able to establish for a transfer between *non-arm's-length* parties that:

1. the transfer was at undervalue; and
2. the debtor was insolvent at the time of the transfer or was rendered insolvent by it *or* that the debtor intended to defraud, defeat or delay a creditor,

then the look-back period is extended from one year to five years.

TRANSITIONAL PROVISIONS

The changes to the "Settlements and Preferences" section of the *BIA* were initially amended pursuant to ss. 72 to 76 of Chapter 47. Further amendments to the changes resulted from Chapter 36. Pursuant to s. 133 of the transitional section of Chapter 47, the changes to the "Settlements and Preferences" section of the *BIA* (ss. 72 to 76 of Chapter 47) are applicable only to a person who, on or after the day on which the amendment comes into force –

- (a) becomes bankrupt;
- (b) files an NOI;
- (c) files a proposal without having filed an NOI;
- (d) a proposal is made in respect of the person without the person having filed an NOI;
- (e) an interim receiver is appointed in respect of the person's property and all or part of the person's

property comes into the possession or under the control of the interim receiver; or

- (f) all or part of the person's property comes into the possession or under the control of a receiver.

The transitional provision indicates that only those debtor companies which trigger one of the above listed bankruptcy events after the amendments to the *BIA* are in force will be subject to the new provisions. This would seem to indicate that a debtor company that becomes a bankrupt before the amendments came into force *will not* be subject to the new remedies provisions even if the transaction in question comes under attack *after* the amendments came into force.

SECTION 50(10)(B)

Subsection 50(10) of the *BIA* governs the trustee's responsibility to monitor and report on the company's actions. The amended subs. 50(10)(b) now requires trustees to report on the reasonableness of a decision to include in a proposal a provision that ss. 95 to 101 do not apply in respect of the proposal.

B. *CCAA*

Mirroring the *BIA*, Chapter 36 creates a new s. 36.1 under the *CCAA* entitled "Preferences and Transfers at Undervalue". The section adopts s. 38 and ss. 95 to 101 of the *BIA* in the context of a compromise or arrangement, unless the compromise or arrangement provides otherwise. It is important to note that subs. 36.1(2) clarifies that any reference to the "date of the bankruptcy" found in ss. 38 and 95 to 101 of the *BIA* is to be read in the context of the *CCAA* as a reference to the "day on which proceedings commence under this Act."

Transfers at undervalue are also dealt with in the newly created s. 60 of the *CCAA* – Credit for Recovery in Other Jurisdictions. Subsection 60(1)(b) provides that when making a compromise or arrangement the value of any property of the company that a creditor acquires outside Canada by way of a transfer that, if it were subject to the *CCAA* would be a preference over other creditors at undervalue, will be taken into account in the distribution of the dividends to the company's creditors in Canada as if it was part of that distribution.

Subsection 23(1) of the *CCAA*, as enacted, is the parallel provision to subs. 50(10)(b) of the *BIA* and governs the monitor's responsibility to report to the

court on the state of the debtor company's business and financial affairs. Subsection 23(d.1) creates the requirement for the monitor, at least seven days prior to the meeting of creditors, to explain the reasonableness of a decision to include in a compromise or arrangement a provision that ss. 95 to 101 of the *BIA* do not apply in respect of the compromise or arrangement.

VI. RESTRUCTURING OF EXISTING COLLECTIVE AGREEMENTS

A. *BIA* AND *CCAA*

Chapter 47 enacted the parallel sections, subs. 65.12 of the *BIA* and s. 33 of the *CCAA*. The sections set out a process in the insolvency context for the potential renegotiation of collective agreements that attempts to balance both the interests of various labour relations regimes and the federal insolvency regime.

Subsection 65.12 and s. 33 create the right for an insolvent debtor company in respect of whom an NOI or proposal has been filed, or who has filed for protection under the *CCAA*, to open up the bargaining process under a collective agreement to which they are a party should they find themselves unable to reach a voluntary agreement with the bargaining agent to revise the collective agreement. The sections *do not* provide either the debtor company or the court with the power to unilaterally amend collective agreements.

In order to "open up" the bargaining process the debtor company, on giving five days notice to the bargaining agent, must apply to the court for an order authorizing them to serve a "notice to bargain". The court will only authorize the service of a "notice to bargain" when it is satisfied that: (a) the renegotiation of the collective agreement is imperative for the making of a viable proposal or plan of arrangement; (b) the debtor company has made good faith efforts to renegotiate prior to bringing the application; and (c) should the authorization not be given by the court the debtor company will suffer irreparable harm.

If the debtor company is successful in obtaining permission from the court to issue a "notice to bargain" and the parties to the collective agreement subsequently agree to revise the collective agreement, the bargaining agent that is a party to the agreement will have a claim as an unsecured creditor for the value of any concessions under the collective agreement.

Pursuant to subs. 65.12(5) of the *BIA* and 33(6) of the *CCAA*, once a debtor company has been authorized to serve a “notice to bargain”, the responding bargaining agent may apply to the court for an order requiring any person to provide information to the bargaining agent which relates to the debtor company’s business or financial affairs and is deemed to be relevant to the collective bargaining between the debtor company and the bargaining agent. These subsections will now provide the bargaining agent with broad power to access the financial and business records of the debtor company.

VII. NEW RECEIVERSHIP PROVISIONS

The *BIA* previously permitted a secured creditor who is about to send, or has already sent, a notice of its intention to enforce its security under s. 244(1) of the *BIA* to seek the appointment of an “interim receiver” over all or any part of the debtor’s property that is subject to the secured creditor’s security. To obtain the appointment, the secured creditor was required to convince the court that such an appointment was necessary for the protection of the debtor’s estate or the interests of the secured creditor. Section 47(2) of the *BIA* provided that a court could direct an interim receiver to do any or all of the following:

- (a) take possession of all or part of the debtor’s property mentioned in the appointment;
- (b) exercise such control over that property, and over the debtor’s business, as the court considered advisable; and
- (c) take such other action as the court considered advisable. Under s. (c), courts have granted interim receivers broad based powers, and such interim receiverships often continue for indeterminable periods of time.

Following the enactment of Chapter 47 and Chapter 36, the *BIA* was amended to confirm the appointment of an interim receiver to a specific period of time and to specific powers. However, the *BIA* was also amended to include the ability of a secured creditor to seek the appointment of a “national receiver”.

INTERIM RECEIVER

Timeline for Appointment

Section 47(1) of the *BIA* has been amended to provide that the appointment of an interim receiver is for a limited period, until the earliest of (a) the taking possession by a receiver, within the meaning of subs. 243(2) of the *BIA*, of the debtor’s property over which the interim receiver was appointed, (b) the taking of possession by a trustee of the debtor’s property over which the interim receiver was appointed, and (c) the expiry of 30 days after the day on which the interim receiver was appointed or of any period specified by the court.

Scope of Powers

Section 47(2) of the *BIA* has been amended to alter the directions that a court may provide to an interim receiver regarding the actions that the interim receiver may take. Section 47(1)(c) of the *BIA*, which previously provided that the court may direct the interim receiver to “take such other action as the court considers advisable”, has been amended to remove this provision from the *BIA*. In its place, s. 47(1) has been amended to provide that the court may direct the interim receiver to “take conservatory measures” and “summarily dispose of property that is perishable or likely to depreciate rapidly in value”.

Place of Filing

Section 47 of the *BIA* has been amended to provide that an application for the appointment of an interim receiver is to be filed in a court having jurisdiction in the judicial district of the “locality of the debtor”. Locality of the debtor will be defined in the *BIA* to mean the principal place

- (a) where the debtor has carried on business during the year immediately preceding the date of the initial bankruptcy event;
- (b) where the debtor resided during the year immediately preceding the date of the initial bankruptcy event, or
- (c) in cases not coming within paragraph (a) or (b), where the greater portion of the property of the debtor is situated.

*NATIONAL RECEIVER**Appointment*

Section 243(1) of the *BIA* has been amended to provide that, subject to subs. (1.1), on an application by a secured creditor, a court may appoint a receiver to do any or all of the following if it considers it to *be just or convenient to do so*: (a) take possession or all or substantially all of the inventory, accounts receivable or other property of an insolvent person or bankrupt that was acquired for or used in relation to a business carried on by the insolvent person or bankrupt; (b) exercise any control that the court considers advisable over that property and over the insolvent person's or bankrupt's business; or (c) take any other action that the court considers advisable.

Section 243(1.1) of the *BIA* provides that, where an NOI to enforce security has been sent, the court may not appoint a receiver under s. 243(1) before the expiry of the 10 days after the day on which the secured creditors sends the notice unless the insolvent person consents to an earlier enforcement or the court considers it appropriate to appoint a receiver before then.

Security for Fees and Disbursements

Section 243(6) of the *BIA* provides that, if a receiver is appointed, the court may make any order respecting the payment of fees and disbursements of the receiver that it considers proper, including one that gives the receiver a charge, ranking ahead of any or all of the secured creditors, over all or part of the property of the insolvent person or bankrupt in respect of the receiver's claim for fees and disbursements. However, the court may not make the order unless it is satisfied that the secured creditors who would be materially affected by the order were given reasonable notice and an opportunity to make representations.

EFFECT OF AMENDMENTS ON RESTRUCTURING PRACTICE

The amendments to the *BIA* that create a "national receiver" and limit the scope and powers of an "interim receiver" provide a uniform receivership model that can be utilized and enforced across Canada.

VIII. TREATMENT OF EQUITY CLAIMS

The *BIA* and the *CCAA* in their previous forms did not specifically address the treatment of equity claims in *BIA* proposal or *CCAA* restructuring proceedings. Following the enactment of Chapter 47 and Chapter 36, the *BIA* and the *CCAA* have been amended to specifically address the manner in which equity claims are treated in insolvency proceedings.

A. *BIA* AND *CCAA**DEFINITIONS*

The *BIA* and the *CCAA* now provide the following definitions for the terms "equity claim", "equity interest" and shareholder":

"equity claim" means a claim that is in respect of an equity interest, including a claim for, among others, (a) a dividend or similar payment, (b) a return of capital, (c) a redemption or retraction obligation, (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d);

"equity interest" means (a) in the case of a corporation other than an income trust, a share in the corporation — or a warrant or option or another right to acquire a share in the corporation — other than one that is derived from a convertible debt, and (b) in the case of an income trust, a unit in the income trust — or a warrant or option or another right to acquire a unit in the income trust — other than one that is derived from a convertible debt;

"shareholder" includes a member of a corporation — and, in the case of an income trust, a holder of a unit in an income trust — to which this Act applies;

VOTING CLASSES FOR EQUITY CLAIMS

Section 54.1 of the *BIA* and s. 22.1 of the *CCAA* now provide that creditors having equity claims are to be in the same class of creditors in relation to those claims unless the court orders otherwise and may not, as members of that class, vote at any meeting unless the court orders otherwise.

B. BIA

ACCEPTANCE OF A PROPOSAL

Section 54(2) of the *BIA* provides that, with respect to voting on a proposal by creditors, the proposal is deemed to be accepted by the creditors if, and only if, all classes of unsecured creditors — other than, unless the court orders otherwise, a class of creditors having equity claims — vote for the acceptance of the proposal by a majority in number and two thirds in value of the unsecured creditors of each class present, personally or by proxy, at the meeting and voting on the resolution.

POSTPONEMENT OF EQUITY CLAIMS

With respect to bankruptcy proceedings, s. 140.1 of the *BIA* provides that a creditor is not entitled to a dividend in respect of an equity claim until all claims that are not equity claims have been satisfied.

C. CCAA

CLAIMS THAT MAY BE DEALT WITH IN A COMPROMISE OR ARRANGEMENT

Section 19(2) of the *CCAA* provides that a compromise or arrangement in respect of a debtor company may not deal with any claim that relates to certain debts or liabilities listed unless the compromise or arrangement explicitly provides for the claim's compromise and the creditor *in relation to that debt* has voted for the acceptance of the compromise or arrangement. Section 19(2)(d) of the *CCAA* provides that the compromise or arrangement may not deal with any debt or liability resulting from obtaining property or services by false pretences or fraudulent misrepresentation, other than a debt or liability of the company that arises from an equity claim. Thus, a compromise or arrangement may deal with a debt or liability of the company that arises from an equity claim even where the creditor did not vote for acceptance of the compromise or arrangement.

D. EFFECTS OF AMENDMENTS ON RESTRUCTURING PRACTICE

The amendments to the *BIA* and the *CCAA* clarify that equity claims are to be generally subordinate to other claims, although judicial discretion is provided to the court to allow equity claims to vote and be dealt

with in restructuring proceedings where the circumstances warrant.

IX. PROTECTION OF PROFESSIONALS

A. BIA

PROTECTION FROM LIABILITY FOR ACTIONS

After the decision of the court in *GMAC Commercial Credit Corporation — Canada v. T.C.T. Logistics Inc.*, [2006] 2 S.C.R. 123, restructuring professionals were justifiably concerned about the exposure of receivers for successor employer liabilities. Chapter 47 and Chapter 36 responded by broadening both the description of a receiver found at s. 243 of the *BIA* and the protection offered by s. 14.06 of the *BIA*.

Subsection 14.06(1.1) was expanded to protect not just trustees, trustees under a proposal, interim receivers and receivers within the meaning of subs. 243(2), but “any other person who has been lawfully appointed to take, or has lawfully taken, possession or control of any property of an insolvent person or a bankrupt that was acquired for, or is used in relation to, a business carried on by the insolvent person or bankrupt.” The broadening of subs. 14.06(1.1) has afforded privately appointed receivers and secured creditors who take possession of a debtor's property with the same protections as a court appointed officer.

Subsection 14.06(1.2) as amended acts to protect professionals from personal liability, including liability stemming from the designation of “successor employer,” with respect to matters and claims of “employees or former employees of the debtor or a predecessor of the debtor or in respect of a pension plan for the benefit of those employees” that existed or relate to the period prior to their appointment.

It is important to note that the protection from liabilities afforded to trustees and receivers by way of s. 14.06 does not extend to protect trustees and receivers from the statutory liabilities existing under ss. 14.06(2) and 81.2 and now arising under ss. 81.3, 81.4, 81.5 and 81.6, respectively, of the *BIA*. Section 14.06(2) provides for the potential liability for trustees and receivers with respect to environmental matters. Section 81.2 provides for the potential liability of trustees and receivers who take possession over and dispose of inventory protected by the section.

Sections 81.3(5) and 81.4(5) create potential liability for trustees and receivers with respect to unpaid wages. Sections 81.5(3) and 81.6(3) similarly create potential liability for trustees and receivers with respect to unpaid amounts owing under prescribed pension plans.

PROTECTION OF FEES, DISBURSEMENTS AND OPERATING COSTS

Pursuant to the new subs. 243(6) of the *BIA*, the fees and disbursements of a receiver are protected under the proposed amendments to the *BIA*. The subsection provides the court with the power to make any order respecting the payment of fees and disbursements it considers appropriate, including an order granting the receiver a charge for its fees and disbursements, ranking ahead of any or all of the secured creditors, over all or part of the property of the insolvent person or bankrupt; the only requirement being that the secured creditors be given reasonable notice of same and an opportunity to respond.

The new subs. 243(7) of the *BIA* acts to limit the protection offered by subs. 243(6), by limiting the definition of disbursements under subs. 243(6) to *not* include any payments made in operation of the business of the insolvent person or bankrupt. While receivers will therefore not find protection for the costs they incur in operating an insolvent or bankrupt corporation under subs. 243(6), they will find such protection from amended subs. 31(1) of the *BIA*. Subsection 31(1) of the *BIA* has been expanded to give receivers within the meaning of subs. 243(2), along with bankruptcy trustees and interim receivers, borrowing powers and security for costs incurred in operating an insolvent or bankrupt corporation, if authorized to do so by the court.

Proposal trustee's fees and disbursements are protected pursuant to the enacted subs. 64.2 of the *BIA*. The subsection gives the court the authority, on notice to secured creditors, to create an "administration" charge over all or part of the property of a person in respect of whom an NOI or proposal is filed in an amount that the court considers appropriate. This "administration" charge is available to protect the fees and expenses of: (a) the trustee, including any professional engaged by it; (b) any professionals engaged by the insolvent person for the purpose of the proceedings; and (c) any profession-

als engaged by *any other interested person* if the court is satisfied that the security or charge is necessary for the effective participation of that person. The section goes further, allowing the court to order that the "third party" charge rank ahead of the claim of *any* secured creditor.

Proposal trustees do not need court protection for the costs associated with operating an insolvent corporation because typically a proposal trustee does not, nor are they required to, step in and run the business of an insolvent corporation. However, in the event that a proposal trustee found itself operating an insolvent corporation and incurring costs doing same, it is arguable that by operation of subs. 66(1) of the *BIA*, which provides that the provisions of the *BIA* are applicable with the necessary modifications to proposals, the proposal trustee could also make use of subs. 31(1) of the *BIA* to protect its costs.

The restriction formerly found at subs. 197(7) of the *BIA* which prescribed that total legal costs rendered to the estate shall not exceed 10% of gross receipts, less amounts paid to secured creditors, except with approval of the inspectors and the Court, has been removed pursuant to Chapter 47.

B. CCAA

PROTECTION FROM LIABILITY

Similar to subs. 14.06(1.2) of the *BIA*, subs. 11.8(1) of the *CCAA*, as amended, acts to protect monitors from personal liability, including liability stemming from the designation of "successor employer," with respect to matters and claims of "employees or former employees of the company or a predecessor of the company or in respect of a pension plan for the benefit of those employees" that existed or relate to the period prior to their appointment.

PROTECTION OF FEES AND DISBURSEMENTS

Similar to s. 64.2 of the *BIA*, s. 11.52 of the *CCAA* as enacted gives the court the authority, on notice to the secured creditors, to create an "administration" charge over all or part of the property of a debtor company in an amount that the court considers appropriate. This "administration" charge is available to protect the fees and expenses of: (a) the monitor, including any professional engaged by it; (b) any professionals engaged by the debtor company for the

purpose of the proceedings; and (c) any professionals engaged by *any other interested person* if the court is satisfied that the security or charge is necessary for the effective participation of that person. Section 11.52, like s. 64.2, goes further and allows the court to order that the “third party” charge rank ahead of the claim of *any* secured creditor.

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• SOLVENCY PROBLEMS? MAKE SURE TO REACT SWIFTLY •

Claude Paquet and Nicolas Plourde
Heenan Blaikie LLP

In these trying times for our economy and our financial system, every business leader should pay attention to the company’s needs for working capital for the year and prepare for any potential problem related to its lack of liquidities.

With the withdrawal of several financial institutions from the market over the past few months, credit facilities have become assets of great strategic value for numerous companies. The decreasing number of financial institutions still active has also impacted the institutions themselves, since they have had to compromise with customers suddenly unable to turn to other institutions for refinancing.

As a result, financial institutions will probably need to cope with their customers’ cash flow problems for a while. They will have to be tolerant and assist their customers, even though these customers may be contemplating remedies allowed by various laws on insolvency. In such a difficult context, businesses will have to:

1. anticipate their cash requirements by making longer-term cash flow statements;
2. implement better communication with their financial institutions;
3. consult with a restructuring expert;
4. examine all possible scenarios applicable to such a cash flow crisis before making decisions that could result in a withdrawal of financing; and
5. negotiate extended payment terms with their suppliers.

WHAT ARE THE LEGAL REMEDIES?

In Canada, the two main statutes that deal with insolvency situations are the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (*BIA*), and the *Companies’ Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (*CCAA*).

THE *BIA*

First, any restructuring plan must include a sound communication strategy, in order to control its impact on suppliers and customers.

A company that is insolvent, or expects to become insolvent in the very near future, may file a notice of intention to make a proposal with the official receiver. This will automatically block creditors’ claims for an initial 30-day period by staying all proceedings. The court may extend this period by increments not exceeding 45 days, up to a maximum of five months after the expiry of the initial period. A similar protection is allowed against changes to a company’s credit ratings.

Still, from a strategic point of view, financial support is crucial during this period. Therefore, it would be preferable for the company to make arrangements with its financial institutions and obtain a stay to avoid this restructuring process, lest these institutions withdraw their support following the proceedings. Some characteristics of the proposal regime are:

- the proposal may shield the company’s directors against employee claims;
- under certain conditions, leases may be terminated upon simple notice;

- although the restructuring is achieved under the authority and supervision of a trustee, management maintains full control of the company;
- the proposal must be approved by creditors within the six-month extended period after the notice of intention. A majority in number (50% + 1) and two-thirds in value of the creditors' proven claims is required, and the approval must be confirmed by the court.

THE CCAA

In many respects, the *CCAA* is similar to the *BIA*'s proposal regime.

The *CCAA* allows a debtor company to benefit from a stay of creditors' proceedings during the period allowed by the court for the preparation and presentation of a plan of arrangement to its creditors. Contrary to the *BIA*'s regime, the stay of proceedings requires an application to the court.

Aside from the initial 30-day stay of proceedings, no time frame is provided. This absence of explicit criteria allows the courts to render tailored applications.

This flexibility and the courts' "inherent jurisdiction" have allowed judges to render orders that were once considered "innovative", but that eventually became well accepted: DIP financing, orders to protect directors or to facilitate the administration, etc. Pending amendments to the *CCAA* have embodied these practices into the Act.

The *CCAA* is, however, restricted to companies with debts in excess of \$5M. Its inherent flexibility explains why it is the preferred avenue for complex restructurings.

As it is the case with a proposal, the debtor company remains in control of its business, although a "monitor" is appointed by the court to supervise and assist the company during the restructuring.

The arrangement proposed by the debtor company must be approved by a majority in number (50% + 1) and by two-thirds in value of creditors' proven claims. Creditors may be distributed amongst several classes: secured and unsecured creditors, etc. When

the creditors are thus divided, the statutory majority is required for each class.

Once the arrangement has been approved by the creditors, it must be sanctioned by the court. If either the creditors or the court rejects the arrangement, the debtor company loses the benefit of the protection of the *CCAA*. Unlike the *BIA*, the *CCAA* does not provide for the debtor's automatic bankruptcy. Still, this outcome is foreseeable in the short or medium term, since the company is usually left with no other choice but to make an assignment in bankruptcy, if a creditor has not already decided to force it into bankruptcy.

CONCLUSION

In the current period of economic woes, numerous companies facing cash flow problems are considering the remedies allowed by the *CCAA* or the *BIA*. These statutes are important tools, and debtors should not be reluctant to use them. However, it is not always necessary to go to that length. An informal reorganization outside the statutory framework of the *CCAA* or the *BIA* may sometimes be possible. In some situations, however, these remedies will be inevitable. In such cases, it is crucial to act swiftly and consult your lawyers and financial advisors before it is too late.

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