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THE INSOLVENCY VERSION OF "SHOW ME THE MONEY"

An Overview of Maximizing Realizations Through Asset Sales

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In any commercial sale transaction, achieving the maximum value involves the primary goal of securing the highest purchase price possible for the conveyed assets. While the purchase price is an important factor in transactions involving the sale of assets of an insolvent entity, there is significantly more emphasis on enhancing value by an appropriate sale strategy and on minimizing costs and other obligations that may affect net recoveries to the stakeholders.

When a solvent company enters into a sale transaction with a purchaser it is typically a bilateral process that can be characterized as having extensive due diligence, generous timelines and a vendor that will continue to exist to the extent certain conditions, representations or warranties subsequently become an issue. On the other hand, a transaction involving the assets of an insolvent company generally involves numerous parties with direct and indirect competing interests, urgent timelines, deteriorating assets and a debtor on the verge of extinction. Insolvency practitioners need to be familiar with concepts such as the choice between a private and a court-appointed receiver, the term "as is, where is", the "vesting" of assets, the staying of proceedings, mandatory supply provisions, the ability to reverse priorities and other issues not present in non-insolvency sales. The process itself involves a number of potential liabilities which, without due care, may lead to significantly diminished recoveries.

In an insolvency transaction, practitioners and stakeholders should appreciate the difference between "show me the purchase price" and "show me the money". Understanding the realities of an insolvent company and selecting the appropriate steps to facilitate a transaction of its assets are fundamental to maximizing the recoveries for stakeholders.

Selection of the Appropriate Legal Framework

The framework for the sale of assets of an insolvent entity has evolved in such a manner that court-supervised realizations have clearly overtaken in popularity private remedies which were much more common 15-20 years ago. There has been widespread acceptance of the view that various elements of the court's involvement add value to the sale process and thereby facilitate maximum recoveries.

The assets of an insolvent business are usually subject to some form of security and the secured creditors have significant influence on the insolvency process. Accordingly, the choice at the outset of a contemplated sale of assets of an insolvent entity is generally between a secured creditor enforcing its security (directly or through the appointment of a receiver) or seeking the appointment by the court of a receiver, interim receiver or liquidator. A sale of assets by a

trustee in bankruptcy typically occurs in the limited circumstances of the debtor having unencumbered assets or, in the cases of secured assets, where the secured creditor is prepared to have the trustee act as its agent.

(i) Private Enforcement

A couple of decades ago, many secured lenders believed that the most economic and efficient method of selling assets of an insolvent business was for the secured creditor to exercise its contractual or statutory remedies directly or through a private receiver. As a result, the majority of receiverships were private through an appointment by a secured creditor.

A private sale is essentially a self-help remedy where the sale is made by a secured creditor or by a receiver appointed by the secured creditor pursuant to the terms of the security. In the case of a private receiver appointed by a secured creditor, it is an agency relationship and typically there is an express written indemnity by the secured creditor in favour of the receiver for liabilities that may arise during the course of the receivership. The power of the secured creditor or receiver to take possession, collect and sell the assets of the debtor is generally set out in the security instrument. If there is no such provision in the security document, the secured creditor or receiver are nevertheless able to sell property pursuant to a statutory power of sale under personal property or real property legislation.

Prior to any enforcement, a secured creditor has statutory and common law requirements to give notice. In addition, prior to the sale of assets, the secured creditor or its receiver are required to give statutory notice to the debtor and other creditors with an interest in the collateral (in the case of personal property, under the provisions of the *Personal Property Security Act* (the "PPSA"), and in the case of real property, under the provisions of the *Mortgages Act*) in order to provide such parties with the opportunity to redeem or, at least monitor the sale.

Subsection 63(2) of the PPSA provides that a secured creditor may dispose of the collateral by public sale, private sale, lease or otherwise so long as every aspect of the disposition is commercially reasonable. There is no requirement that a secured creditor or private receiver obtain the approval of the court in respect of the marketing or sale of the assets. The safeguards lie in the statutory and common law obligations that could give rise to a claim for improvident realization. While "commercial reasonableness" is not defined, the case law suggests that a commercially reasonable sale will be one that uses the method best suited to the sale of the particular property in the circumstances. The courts have held that, for a disposition to be commercially reasonable, the secured creditor must meet the objective standard of reasonable care and the subjective standard of good faith. Obviously, the main factor in determining commercial reasonableness is the price paid for the collateral. Therefore, obtaining appraisals or other persuasive evidence of value is prudent in order to protect against a claim that the sale was improvident.

Finally, it should be noted that a secured creditor or privately appointed receiver may seek the assistance of the court in cases where the debtor is resisting the enforcement or to obtain the benefit of the court's advice and directions. In addition, there have been circumstances where

a secured creditor has attempted to seek the court appointment of a receiver after an initial private appointment. The conversion of a private receiver into a court-appointed receiver has been successfully resisted in some courts on grounds that, absent compelling reasons, the court should not intervene once the secured creditor has made its election in favour of a private receiver. That being said, the involvement of the court in the private sale process or a conversion to a court-appointed receivership will likely undermine the principal advantage of a private sale, namely a less costly enforcement mechanism.

(ii) Sale by a Trustee In Bankruptcy

As noted above, the sale of assets by a trustee in bankruptcy usually occurs in the limited circumstances where there are unencumbered assets or where the secured creditor authorizes the trustee to sell the collateral as its agent (i.e. receiver). For the most part, a sale of unencumbered assets by a trustee is made pursuant to its statutory powers with limited involvement of the court. Under the provisions of the *Bankruptcy and Insolvency Act* (the "BIA"), the trustee may, with the permission of the inspectors, sell or otherwise dispose of the assets of the estate. The trustee may offer the assets of the estate for sale by tender, public auction or private contract. This flexibility allows the trustee to select an appropriate marketing and sale mechanism for the assets of the estate subject to the guidance of the inspectors. Notwithstanding the involvement of the inspectors, the trustee has statutory obligations of good faith and commercial reasonableness such that the trustee's actions are still subject to challenge by interested creditors.

As a result of the limited scenarios where there are meaningful unencumbered assets, sales by trustees have become infrequent. Secured creditors are generally predisposed to controlling the sale of their own collateral either directly or through a receiver of their own choosing. In addition, there may be concerns that a sale of secured assets by the trustee will subject the proceeds to the superintendent in bankruptcy's levy pursuant to the BIA. Nevertheless, there are circumstances where a bankruptcy proceeding is advantageous in conjunction with a private or court-appointed receivership. Firstly, a strategic bankruptcy can reverse certain statutory priorities, such as the deemed trust for GST arrears, with the effect that the proceeds of the sale of assets are maximized for the benefit of the other creditors. Secondly, a trustee in bankruptcy has statutory rights with respect to leased real property. The ability of the trustee to occupy the premises for a period of time is something that is not available to a privately appointed receiver and may be crucial if the receiver needs time to sell the assets. Moreover, the trustee has the ability to assign a lease that may have value as a stand-alone asset or as part of the sale of a turn-key operation. Neither a private nor a court-appointed receiver has the statutory power to assign leases over the objection of a landlord.

(iii) Court Supervised Sales

For a number of reasons, the practice has significantly shifted away from private receiverships to court supervised realizations by a receiver appointed under a provincial statute (*Courts of Justice Act* in Ontario). In addition, there has been a dramatic rise in the use of interim receivers appointed under the BIA, particularly in order to facilitate asset sales in the context of reorganization proceedings.

Unlike a private receivership or an assignment in bankruptcy, the commencement of a court-supervised receivership involves an application to the court for the appointment of the receiver and, if the order is granted, the receiver's powers are derived solely from the court order. An initial receivership order typically includes authorization for the receiver to take possession of a debtor's assets and to carry on its business. In addition, the practice is to grant broad stays of proceedings against all creditors and suppliers in order to prevent various enforcement actions, the interruption of the supply of goods and services and the termination of agreements, leases or licenses. There are also provisions that provide expansive protection for the receiver from various statutory liabilities such as successor employer issues and environmental concerns. Finally, a receiver will have authority to pursue, consider and develop sale options and to market and sell a debtor's business and/or assets, subject to court approval.

The complexity of commercial enterprises and exposure of the receiver (and ultimately the appointing creditor) to liabilities are among the principal reasons why court supervision is viewed as adding value to the realization process. In terms of complexity, many insolvent companies have numerous creditors, often in many jurisdictions, with different rights, remedies and priorities against the debtor's business and assets. As noted above, provisions for the stay of proceedings, mandatory supply and interim financing, prevent individual creditors from taking self-interested actions and provide a controlled environment within which to sell the assets. A court-supervised proceeding also generally represents the best opportunity to sell the business as a going concern. Businesses are generally worth more than the sum of their parts and therefore, a realization strategy should explore the benefits of marketing the assets as a whole.

Many realizations today occur within the context of a reorganization proceeding. In part, the courts have recognized that a sale of a business or various assets within a proceeding under the *Companies Creditors' Arrangement Act* (the "CCAA") or a proposal under the BIA may be the only realistic opportunity to restructure a "business" and for stakeholders to achieve a meaningful recovery. The actual or apparent attempt at reorganization also adds value when contrasted to a receivership or bankruptcy sale with a terminal outcome. The perception that there are other options may very well attract higher bids for the business or assets.

A secured creditor or its privately appointed receiver have limited protection against numerous statutory liabilities and are subject to claims of third parties based on the sales process, the sale price and the distribution of proceeds. The irony is that by trying to keep costs down by avoiding the court process, the secured party may find itself facing increased exposure and more expensive litigation dealing with the sales process after the fact. On the other hand, the orders appointing receivers have expansive protections for court appointed officers against statutory liabilities. In addition, the court's approval of the various steps in the marketing and sale of the assets effectively cuts off protracted litigation over such issues.

Finally, the added value of a vesting order made in a court-supervised realization cannot be over emphasized. In circumstances where the ability to conduct due diligence is limited, both in terms of available time and often inadequate records of the debtor, an order vesting the assets in the purchaser, free and clear of all encumbrances and claims, is the most effective answer to a purchaser seeking some comfort in a no recourse transaction.

While a private receivership is still arguably less expensive, the complexities and risks inherent in today's insolvency environment generally result in the selection of a court supervised process in all but the most simple of insolvency transactions.

Marketing and Sale of the Business or its Assets

There is no single procedure that is appropriate for the marketing and sales process in respect of the assets of an insolvent enterprise. Rather, there are guidelines based upon the business realities, common sense and commercial reasonableness. While the relevant duties and obligations of the private receiver and trustee generally arise from the statutory regime and the court-appointed receiver from the receivership order, in practice the considerations and procedures for marketing the assets of an insolvent entity are similar. The main difference is that the private receiver and trustee are susceptible to challenge of their actions after the fact, whereas a court-appointed receiver relies upon court approval before taking a step. Under either scenario, the marketing and sale of assets involve aspects of commercial reasonableness.

The nature of the marketing and the selection of a process for offering the assets for the sale to potential purchasers generally depend upon the specific circumstances of each insolvency and the industry in which the business operates. With this in mind, the general considerations for the process of marketing and selling include:

- (i) an appropriate marketing strategy given the nature of the assets and the particular industry;
- (ii) an appropriate timeline for exposure of the assets;
- (iii) use of a tender, auction or other sale process that is appropriate in the circumstances;
- (iv) the integrity of the process by which offers are obtained;
- (v) the merits of continuing to operate the business in an effort to achieve a going concern sale; and
- (vi) the interests of the parties in the assets and the proceeds.

The receiver or other applicable vendor will consider the best advertising methods as part of its marketing strategy. The receiver will often advertise in specific industry publications in the case of non-consumer assets and in media reaching a more widespread audience in the case of consumer assets. In circumstances of a going concern sale, the receiver will consider marketing to the applicable industry or the investor community. There should be a cost-benefit analysis in order to balance the desire to "cast the net" widely enough to attract the highest number of bidders against the pressure to avoid wasted costs. In part, practitioners must rely on the expertise of those people involved in a particular industry to determine and justify the appropriate course of marketing the assets. The same principles hold true in terms of determining the appropriate length of time for marketing the assets, particularly when the assets may be deteriorating or the carrying costs will erode the eventual recoveries.

An asset sale may be made through an auction, tender or other sale process. This is the area where significant attention is required to ensure that the process is fair to all interested parties. In part, the selection of the sale mechanism will be dictated by the nature of the assets and the specific industry. For example, an auction may be the most expeditious and cost effective method to dispose of individual assets or groups of equipment, furniture and fixtures. In addition, an auction may be considered to sell remaining assets after the majority has been sold through some other process. A tender sale in its traditional sense involves a tender package that sets out the assets, the terms of sale and a deadline date for the opening of tenders. The successful purchaser will be the one with the highest tender when the tenders are opened. Nevertheless, with the complexity of asset sales and the various issues subject to negotiation, strict tenders are rarely used.

When dealing with significant parcels of assets or a going-concern business, the more common approach is through a process that calls for "expressions of interest" followed by further negotiations and ultimately selection of the best deal. While such processes have been referred to loosely as "tenders" or "bids", they are more informal and flexible. In cases where there may be numerous bidders or complex transfer issues, the receiver will typically prepare an information package including a full description of the assets, the mechanics of the bidding process (including the deadline for receiving bids), a confidentiality agreement and a form of offer to purchase with requisite terms and conditions. As will be discussed below, the terms usually provide that there will be no representations or warranties made by the receiver in respect of the assets and the sale will be made on an "as is, where is" basis. By including the "standard" terms and conditions (or in some cases, the required form of asset purchase agreement), the receiver will be able to compare bids primarily on the basis of net proceeds as opposed to sifting through numerous conditions. Finally, the bid package usually contains a term that the receiver is not bound to accept the highest bid (if there are concerns about the bidder's financial ability or its imposition of onerous conditions) or any bid (if all of the bids are unsatisfactory).

The receiver usually will reserve the right to go back and enter into discussions with certain of the bidders with a view to clarifying bids in order to arrive at a transaction that is both more certain to close and represents the best recovery. This must be differentiated from "shopping bids", which is a process of taking the best bid to other parties to see if they will bid more. Shopping bids is generally viewed as unfair and inappropriate in Canada. While many bid processes involve a second round of negotiations on the basis of clarifying or eliminating conditions in various offers, the receiver must be careful to ensure that the integrity of the process is not compromised.

Unlike Canada, the common practice in the U.S. is that of a controlled bid shopping process through the use of a "stalking horse". In Chapter 11 proceedings, the usual procedure is for the debtor to negotiate a sale price with an interested purchaser, on the condition that if the debtor does not complete the deal, it will pay a specified "break-up" fee to the would-be purchaser. The debtor then obtains a court order setting a date for approval of the transaction and also authorizing the debtor to circulate the stalking horse bid to all of the creditors and interested parties, stipulating that any interested bidder has the opportunity to submit a "minimum overbid". The minimum overbid is usually required to be an amount in excess of the initial bid and the break-up fee. Potential bidders then have the opportunity to submit competing bids and, if more

than one bidder submits a minimum overbid, the court will order that an auction be conducted among the bidders.

The "stalking horse" method has been used in Canada in cross-border proceedings involving a sale *en bloc* of U.S. and Canadian assets. For instance, in the PSINet insolvency, assets were owned in part by the Canadian applicants under the CCAA filing and in part by their U.S. parent PSINet Inc. that was operating under Chapter 11 proceedings. Justice Farley held that it was practical in the circumstances to employ the U.S. process and approved the sale of PSINet's Canadian assets to Telus Corporation pursuant to that process.

Given that Canadian courts generally do not approve of "shopping bids" on the basis that it violates our principles of procedural fairness and the role of receivers as court officers, it is unlikely that the courts would approve a "stalking horse" sale involving solely Canadian assets. That being said, there have been a number of cases where a receiver is appointed to complete a sale transaction that has been negotiated by the debtor and the circumstances (intentionally or unintentionally) may give rise to a form of stalking horse. It is typical in many forbearance agreements that the debtor is encouraged to explore opportunities to sell all or part of its business subject to the secured lender's approval. If the debtor brings a deal to the secured lender, a receivership may be necessary to provide a mechanism to convey the assets. The receiver, particularly a court-appointed receiver, may recommend a further sales process in order to satisfy itself that the proposed transaction is the best option. Absent confidentiality provisions, the pre-receivership purchaser in effect becomes the stalking horse. At a minimum, the pre-receivership deal provides the receiver with the basement purchase price.

The relative interests of various creditors or other parties may also play a significant role in establishing an appropriate marketing and sale process. Where there is a clear indication that the primary secured creditor is going to suffer a shortfall in its recovery, the support of such party for the process is critical and may justify an abbreviated process, where such creditor simply wants to "get the deal done", or a more elaborate procedure if it believes that a better deal may be available. On the other hand, where it appears that there will be a surplus of the realizable assets over the senior lender's position, the receiver should attempt to obtain a consensus among the broader constituency with an economic interest. The merits of continuing to operate a business is a consideration that depends upon the party or parties financing or bearing the cost of such continuance as well as the parties who may be the beneficiaries of an enhanced recovery. Other third party interests may be relevant as well. For example, in cases where the products manufactured by an insolvent business are subject to licenses, a prospective purchaser may well have to be acceptable to the licensor, and in such case, maximizing the realization would necessarily involve input from the licensor.

Before leaving this section, it is worth noting that there are asset sale scenarios where a marketing process is unnecessary and does not add value to the recovery. In these circumstances, maximizing recovery involves avoiding costs that would otherwise reduce the net proceeds. Transactions where there is no sale or marketing process have been referred to as "quick flips", which typically involve a secured creditor selling the assets to a "newco" controlled by parties related or friendly to the former owners, or "pre-packs", which involve a sale that is pre-negotiated by the major stakeholders subject to the court's approval. In either case, the "business" continues with minimal disruption. Such transactions often appear as

sinister to third party creditors who see little recovery or other parties who would have liked the opportunity to bid on the assets. Nevertheless, it is difficult to challenge such sales where the complaining creditors were unlikely to see a recovery in any event and the transaction was acceptable to the stakeholders with a direct interest. In order to protect the parties involved in the transaction, there should be evidence that the net purchase price is reflective of the value of the assets such that there would be no advantage to a further marketing or bid process. Such evidence is typically in the form of independent appraisals of value. In cases where the secured creditor is facing a shortfall, the quantum of the actual shortfall is relevant in establishing that any sale or marketing process would likely not benefit other creditors. Finally, quick flips or pre-packs may also be advantageous where the assets are rapidly deteriorating in value. In most cases, an insolvent business is very fragile and the negative impact of a protracted insolvency proceeding can significantly diminish its goodwill or other values. In the appropriate circumstances, such transactions not only maximize recovery by avoiding unnecessary costs but preserve value.

Negotiating the Sale Agreement

Once the process moves to the stage of negotiating a definitive asset purchase agreement, there are a number of factors in the formulation of an asset purchase agreement that are relevant in order to maximize the realization from an asset sale. The overriding principle is that comprehensive negotiations and careful drafting are necessary to ensure that the recovery contemplated in an acceptable bid becomes the actual net proceeds recovered by the receiver pursuant to the asset purchase agreement. With this in mind, it is worthwhile to consider the perspectives of the receiver, as vendor, and the purchaser in terms of the formulation of the asset purchase agreement.

A receiver generally has two main concerns when formalizing the sale transaction: (i) certainty that the deal will close within a reasonable time frame; and, (ii) minimizing the conditions and potential liabilities that may reduce the effective recovery. On the other hand, it is obvious that the purchaser's goal is typically to buy the assets of an insolvent business for a "distress" price. While generally agreeing with the terms of a no recourse sale, the purchaser will use every effort to insert provisions that will further reduce the purchase price or will protect it from post-closing uncertainties. One common misconception is that a bid with an acceptable purchase price is easily reflected in a definitive sale agreement. The reality is that in the majority of cases, the purchase price is subject to revision as the parties identify various conveyance issues. Unfortunately for receivers, the purchase price rarely goes up in such circumstances.

With these perspectives in mind, it is useful to review certain issues and provisions that frequently arise in the context of negotiating an asset purchase agreement involving the assets of an insolvent business. In addition, a sample asset purchase agreement is attached as Schedule "A" to this paper for purposes of reviewing common provisions found in such agreements. While a number of the following issues are typical of an insolvency transaction, the listed topics are by no means exhaustive. Some will be more contentious than others depending upon the nature of the assets or business being conveyed.

- (a) "As is, where is": No Representations or Warranties

In almost every agreement for the conveyance of assets of an insolvent entity, there is a provision that purchaser has inspected the assets, is accepting them in their existing condition and where they are located ("as is, where is") and that the vendor makes no representation or warranty with respect to title, description or purpose, quality or quantity or merchantability of the subject assets. In addition, there is typically a limitation of the conveyance to "the interest of the debtor, if any, in the purchased assets".

The "as is, where is" condition and the refusal of the vendor to give representations and warranties are practices which are necessary to allow for the timely completion of an insolvency proceeding and to secure certainty relative to the net recovery. These principles arose from the need of trustees to be able to close down bankruptcy estates within a reasonable period of time. When trustees or receivers are faced with potential subsequent claims arising from an asset sale, there will also be increased professional costs and diminished recoveries (as well as potential delays in distributions). In addition, trustees and receivers (or secured creditors) are selling assets that they themselves did not acquire, manufacture or use. Accordingly, they are not capable of making informed representations regarding the assets. They are also not in a position to deal with warranty issues. It is more appropriate to give the purchaser the opportunity to inspect the assets and conduct any other due diligence it wishes. Any deficiency or risk associated with the assets is in part already reflected in a discounted purchase price. In the end, this practice allows the receiver to ensure a relatively predictable recovery without the prospect of subsequent claims that would delay or reduce distributions to stakeholders.

The rise in popularity of vesting orders has been an advantage to both purchasers and vendors. Most purchasers without any prior insolvency experience have great concern over the concept that they are buying the debtor's interest "if any" in the assets. As noted above, this risk is partially addressed by the reduced purchase price. Nevertheless, when a purchaser is leveraging such risks in favour of further reductions to the purchase price, the vendor may take the position that many of such concerns can adequately be addressed by a vesting order. Although vesting orders are discussed in more detail below, they are somewhat of a balance to the "as is, where is" provision. Vesting orders provide comfort to purchasers in terms of title issues and the prospect of future claims against the purchased assets. A vesting order also addresses the purchaser's anxiety over the lack of representations and warranties in respect of title issues and encumbrances that are typically present in non-insolvency transactions.

While the practice of vendors not providing representations or warranties has been widely accepted, it should be noted that it is not an absolute rule and there may be particular circumstances where recoveries may be enhanced by deviating from this practice. One example is the case where the major secured creditor is also the principal supplier of inventory to the debtor company. In such circumstances, the secured creditor may be prepared to warrant the condition of the debtor's inventory in order to secure an increased purchase price. Moreover, it is becoming more common to see risk sharing arrangements, such as splitting the proceeds of accounts receivables collected by a purchaser once they exceed a certain threshold, as opposed to a simple transfer of the receivables for a lesser purchase price. Similarly, the provision of indemnities is typically an issue of contention between the parties. However, an indemnity (by or in favour of the receiver) may be necessary to complete a transaction and enhance value in certain circumstances. Although there are general concepts applicable to insolvency

transactions, practitioners should not be so tied to these concepts that they miss opportunities to enhance the recovery from an asset sale.

(b) Employee Issues

The employees of an insolvent debtor are often important to the sale of the debtor's assets. However, they are also the source of considerable anxiety in the sale of an insolvent business. The receiver will wish to avoid successor employer obligations and other employee related liabilities while it its operating the business and completing the sale.

The starting point is an appreciation of the actual exposure in respect of employee obligations. Where there is no collective agreement, a receiver who attempts to continue the business of a debtor in order to seek a buyer for the business as a going concern will generally not be considered to have assumed the debtor's liability for severance and termination pay in the event that a sale cannot be completed and the business is ultimately liquidated. The receiver's obligations will typically be limited to paying the employees for their services during the period of the receiver's operations. The issue is more complicated in the case of unionized employees. The *Labour Relations Act* provides that any person to whom a business is "sold" by an employer is bound by any collective agreement between the employer and its employees. The definition of "sells" includes leases, transfers and any other manner of disposition. The concern is that the receiver's control of a business may be considered a transfer under this definition. In a private appointment, the security agreement typically provides that a receiver appointed by the secured creditor will carry on the business of the debtor as the agent of the debtor. This agency concept has been accepted by the courts as effective to protect privately appointed receivers from any claim that they have received a "transfer" of the business for the purposes of the *Labour Relations Act*. However, court-appointed receivers are not agents but independent court officers, and courts have held that they receive a transfer of the business for *Labour Relations Act* purposes unless the order specifically provides otherwise.

As additional protection for receivers, there is often the express termination of a debtor's employees in receivership orders accompanied by an authorization for the receiver to temporarily contract with some or all of the former employees. Alternatively, a bankruptcy also has the effect of legally terminating the employment relationship. In the case of an interim receiver appointed in conjunction with a reorganization proceeding, it can be made clear that the debtor maintains its role as the employer while it remains in possession and control of its business. As a result, the interim receiver should have no liability in respect of the debtor's employees. This is similar to the cases of an interim receiver transferring the property of a debtor without actually going into possession of such assets in order to avoid environmental issues. Notwithstanding such efforts, in any case where the receiver is retaining the services of the employees, it is prudent for the receiver to make it clear in writing to the employees that they are temporary independent contractors pending a sale or liquidation of the business.

In order to assess the merits of maintaining the workforce or specific employees, the receiver should evaluate the benefits of having former employees complete contracts or work in process. The receiver should also consider the prospects of selling the business as a going

concern and the necessity of the employees as part of the package. The receiver has an opportunity to recover value by facilitating the transition of some or all of the employees to a purchaser of the business. If the receiver ceased operations, a purchaser of the "hard" assets would be able to hire a number of the employees without any consideration flowing to the receiver. In many cases, that is exactly what the purchaser wishes to do. The receiver must both recognize the value of the employees to a prospective purchaser of the business and try to take advantage of its position of having temporary control over the workforce. A receiver should also use its ability to facilitate the transfer of selected employees (as opposed to the entire workforce) as leverage in the bargaining process.

From the perspective of a purchaser, the statutory regime relating to employees often causes undue concern. The purchaser should accept the fact that it will assume the successor employer obligations of those employees it wishes to hire. The "value" is its opportunity to shed the "business" of unwanted employees without incurring any obligations in respect of the employees that it does not hire. As part of its due diligence, the purchaser should identify those employees it believes are critical for the continuation of the business and ensure the debtor's current obligations to such employees for wages and statutory remittances are up to date. Nevertheless, purchasers typically seek all types of representations and indemnities regarding employees. Receivers often find themselves having to educate purchasers as to employee liabilities in order to avoid unnecessary indemnities. As a partial response, receivers should have no difficulty including a "motherhood" clause in the asset purchase agreement that the purchaser is not assuming any obligations of the debtor business other than as expressly set out in the agreement, and in particular, in respect of any employees the purchaser does not hire.

Finally, the receiver may attempt to "download" some of the obligations or costs relating to employees to the purchaser. For example, where there is a potential for recovery by unsecured creditors of the debtor, encouraging the purchaser to hire all or most of the employees will reduce the employee claims against the estate and thereby enhance recoveries for the remaining unsecured creditors. In addition, where the purchaser is anxious to preserve critical employees, it may be prepared to bear some of the cost of keeping such employees associated with the business pending the completion of a transaction.

(c) Transfer of Contracts

The primary goal of a receiver is to negotiate an agreement that will recover value from the debtor's "equity" in various contracts. Where the contract merely represents a debtor obligation, the receiver may want to facilitate its transfer in order for the purchaser to assume an obligation that may otherwise have to be dealt with or simply leave it out of the transaction if the associated transfer costs will significantly impact on the net recovery. On the other hand, the purchaser has the opportunity to leave behind assets that it does not require or that may involve an assumption of obligations that are not cost effective. For instance, the debtor may have a leased machine that the purchaser can obtain from another lessor on more favourable terms. The same may hold true for certain executory contracts that may not be profitable.

An important issue is whether the contracts, leases or licences of an insolvent company can be effectively assigned to the purchaser. Many have assignment restrictions that either

absolutely prohibit their assignment or require the consent of the current counter-party. Accordingly, purchase agreements involving such assets typically include a provision that the contracts are being assigned to the extent that they are assignable and that the vendor will use all reasonable efforts to assist the purchaser in obtaining the assignment. While such a clause goes part of the way, the reality is that most assignors will be prepared to consent to their contracts being assigned to a creditworthy purchaser provided that any arrears are paid up to date. As a result, responsibility for the payment of arrears usually becomes the contentious issue. While the receiver will attempt to have the purchaser assume this liability, such payment is often negotiated on the basis of the relative importance of the contract to the purchaser and the impact of the payment of the arrears on the net proceeds of the transaction.

As noted in the section on sales by trustees, the trustee's ability to occupy leased premises and assign real property leases without the landlord's consent provides the trustee with additional rights not possessed by receivers. Notwithstanding the provisions of any lease, if the debtor makes an assignment under the BIA or if a receiving order is made with respect to its property, the *Commercial Tenancies Act* provides for a trustee's right of occupation for a period up to three months. In addition, if the trustee elects to retain the lease, it may assign the lease to a purchaser who undertakes to be bound by the terms of the lease and to carry on in the premises a business that is not more hazardous or objectionable than the bankrupt's business.

As a result of the trustee's rights of occupation and assignment, in cases where there is an uncooperative landlord or the premises are critical to a controlled realization or going concern sale, there may be significant added value in effecting the debtor's bankruptcy or coupling a bankruptcy with a receivership proceeding. The latter would facilitate a receiver's sale of the assets of the business and the trustee's assignment of the leased premises to the same purchaser.

One final matter of note is the manner in which assignments of contracts and leases were dealt with in the recent CCAA proceedings involving the Ottawa Senators. In the context of an order approving the proposed sale of the hockey team, there was a provision in the order that contracts were "deemed" to have been assigned to the purchaser unless any party to the contract filed an objection by a specified date. Among the problems inherent with large transactions involving numerous contracts are the cost, time and complexity of negotiating consents to hundreds of assignments. The effect of the provision in the Ottawa Senators sale approval order was a reversal of the onus of securing an assignment and placing the burden on the counter-party to a contract to object to the proposed assignment. While the court's jurisdiction to override contractual provisions in such circumstances may be questioned, the result was advantageous to both the vendor and the purchaser (particularly, with the possibility that liability for arrears was left as an obligation of the insolvent debtor company). At a minimum, such a provision may provide leverage to the vendor when dealing with counter-parties to contracts.

(d) Selling the "Name"

Depending upon the circumstances, the value of a name, trademarks and phone numbers of a business may be significant. In the case of a name with widespread public recognition, there is value in the ability of a receiver to transfer it to a purchaser.

The concern of a purchaser is to ensure it acquires exclusive rights to the name. Ultimately, a complete transfer by the receiver of its interest in the name to the purchaser and the debtor changing its name to a numbered company provide the greatest value to a purchaser. However, in many instances all of the directors of an insolvent company have resigned so that the debtor cannot amend its articles. There are also practical problems in changing a debtor's name while an insolvency proceeding is ongoing or a bankruptcy estate is being administered.

One of the solutions is not to change the name but to have the vendor provide an undertaking that, following closing, the name will only be used in respect of administration of the estate and not for any commercial purposes. Another previously successful approach in the case of receiverships is to seek a provision in the sale approval order that would authorize and direct the receiver to execute articles of amendment for the name change. In any event, the main challenge is to find a practical solution that facilitates the transfer of the name in such a fashion that the purchaser cannot argue that a partial transfer diminishes its value.

(e) Approval and Vesting Orders

Generally the ability to obtain court approval of the sale and a vesting order is limited to court-supervised realizations. The asset purchase agreement usually includes a term that the vendor will apply to the court for both an order approving the sale and an order vesting the assets in the purchaser free of claims. The approval order typically has a number of provisions that assist the conveyance, such as deemed compliance with, or waiver of, statutory requirements. As already noted, approval and vesting orders are efficient mechanisms for conveying assets and represent significant "added value" to an insolvency transaction.

On the application for approval, the court generally follows the recommendation of the receiver unless there is a demonstrable flaw in the process or the court is concerned that the recovery is not commercially reasonable. Accordingly, the receiver has both a duty and the advantage of only recommending a transaction that it believes is in the best interests of the stakeholders and is commercially reasonable. Unlike an ordinary commercial transaction where a vendor may be pressured to "give" on various issues that involve solely its interest, a receiver has more leverage in terms of its view of the threshold necessary for court approval as well as its duty to "all stakeholders".

The widespread acceptance of approval and vesting orders as conveyance mechanisms and their flexibility in responding to specific circumstances are among the reasons for a shift from private to court-supervised realizations. In part, improved access to the courts, particularly the Commercial List in Ontario, has made the practice more popular. More importantly, vesting orders have become "cure-alls" to purchasers and allowed receivers to continue to resist requests for representations and warranties.

Notwithstanding the popularity of vesting orders, there are issues that practitioners should be aware of. One issue is the effectiveness of a vesting order against parties that were not given notice prior to making such order. It is primarily the responsibility of the purchaser to ensure that all identifiable parties with a potential interest in the conveyed assets are served with the materials supporting the application for the vesting order and thereby, are arguably bound by the terms of the order. The parties to a transaction also often debate the issue of whether the closing

will occur upon the granting of the approval and vesting orders, the expiry of appeal periods or the final disposition of any appeal of such orders. Generally, the receiver is anxious to complete the transaction and there are costs associated with running the operations or storing the assets for a minimum of at least 30 more days. Nevertheless, a cautious purchaser often prevails on this point unless there appears to be no opposition to the sale approval order and it is anxious to take possession of the assets as soon as possible. The same may be true in respect of the timing for the receiver to make distributions of the proceeds following closing of the transaction. Typically, the receiver is required to hold a reserve for post-closing adjustments or will require "claw-back" agreements with the major creditors that receive a distribution.

As already noted, the above represent some of the common issues that arise in the context of negotiating the transfer of assets of an insolvent enterprise. Depending upon the circumstances, there may be other critical issues, such as environmental, tax or regulatory concerns. In any event, it should be recognized that there are ways to constructively address such issues and to facilitate a transaction in which the recovery is maximized.

Conclusion

There are many steps and factors in the process of selling the assets of an insolvent entity that contribute to maximizing recoveries. The purchase price is only one of the concerns. Success in an insolvency transaction requires an appreciation of methods that may enhance value notwithstanding the distress circumstances and, at the same time, minimize risks that drive the price down or expose the vendor to costs or liabilities that effect recovery. Understanding the realities of an insolvent business, the legal options and the issues in negotiating a sale agreement are critical when it comes time for the stakeholders to say "show me the money".