



THE CANADIAN BAR ASSOCIATION  
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## **Submission on Bill C-55 – Bankruptcy Reform**

**NATIONAL BANKRUPTCY AND INSOLVENCY LAW SECTION  
CANADIAN BAR ASSOCIATION**

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## **PREFACE**

The Canadian Bar Association is a national association representing 36,000 jurists, including lawyers, notaries, law teachers and students across Canada. The Association's primary objectives include improvement in the law and in the administration of justice.

This submission was prepared by the National Bankruptcy and Insolvency Law Section with assistance from the Legislation and Law Reform Directorate at the National Office. The submission has been reviewed by the Legislation and Law Reform Committee and approved as a public statement of the National Bankruptcy and Insolvency Law Section of the Canadian Bar Association.



## EXECUTIVE SUMMARY

The National Bankruptcy and Insolvency Law Section of the Canadian Bar Association (the CBA Section) is pleased to present this submission on Bill C-55, which amends the *Bankruptcy and Insolvency Act* (the BIA) and the *Companies' Creditors Arrangement Act* (the CCAA), and creates the *Wage Earner Protection Program Act* (the WEPP Act). Bill C-55 includes important changes to the law, one of the most significant being the introduction of the wage earner protection plan (WEPP). The CBA Section supports this addition and welcomes opportunity to participate in the process of making the law of bankruptcy, insolvency and company restructuring clearer and more effective.

### Commercial Insolvency Summary

**Compensation Protection: Wages and Pensions:** The CBA Section supports the creation of the WEPP. The CBA Section recommends that provisions be added to ensure the payment of fees and disbursements of insolvency administrators in performing duties relating to the charge over the assets of the debtor to secure unpaid/unremitted pension contributions, the super-priority charge to secure unpaid wages and vacation pay (the Employee Charge), and the WEPP, and that they be protected against liability for failure to perform their duties for reasons outside of their control.

The CBA Section further recommends that the insolvency administrator who pays funds to an employee or the WEPP under the Employee Charge be subrogated to any rights the employee might have against the debtor's directors, to minimize the impact of the Employee Charge on other creditors.

**Interim Financing:** the CBA Section generally supports the inclusion of provisions in the BIA and the CCAA with respect to interim financing. The CBA Section recommends that the factors to be considered by the Court in connection with an application to approve interim financing be distilled down to a smaller number of essential factors:

- (a) whether the proposed financing is necessary to allow the debtor to operate;
- (b) whether the proposed financing will enhance the prospects of the debtor being able to make a viable proposal or plan;
- (c) the nature and value of the debtor's assets, and
- (d) whether any creditor will be materially prejudiced by the proposed financing or the security to be provided in connection with the proposed financing.

**Disclaimer of Agreements:** The CBA Section supports amending the BIA and CCAA to permit the disclaimer of agreements. The CBA Section further supports allowing a party to an agreement that the reorganizing debtor is proposing to disclaim to apply for an order that the agreement may not be disclaimed. However, the CBA Section proposes that the party to the agreement be required to establish, in order to obtain the order, that serious prejudice will result from the disclaimer and that the disclaimer is not necessary for the reorganization to be successful.

The CBA Section also believes that changes are required with respect to disclaimers of intellectual property to strike an appropriate balance between the rights of licensees, and debtors. The CBA Section recommends that the amendments:

- provide that the debtor's disclaimer of an agreement granting an intellectual property license to a licensee does not affect the licensee's right to use the intellectual property unless the debtor is able to establish that one of two circumstances exist. The debtor must prove either that the licensee's business will not be adversely impacted by the disclaimer or that it is otherwise appropriate to terminate the licensee's right to use the intellectual property; and
- clarify that the debtor/licensor shall have no further obligations under the repudiated license and is not restricted by any terms of the repudiated license.

**Assignment of Agreements:** The CBA Section notes apparent inconsistencies in the new provisions of the BIA and the CCAA that permit the assignment of agreements, in particular:

- the types of agreements that can be assigned;
- the test to determine if the debtor ought to be able to assign an agreement; and

- the types of defaults that must be cured at the time that the agreement is signed.

The CBA Section recommends that the BIA provisions be parallel to the CCAA provisions.

**Transfers at Undervalue and Preferences:** The CBA Section generally supports the collapse of the settlement and reviewable transaction provisions of the BIA into the single concept of a transaction at undervalue. It also supports the adoption of the term “non-arm’s length” to expand the class of connected parties subject to the one-year look-back period for attacking transactions. The CBA Section recommends that:

- The definition of transaction at undervalue provide that any transaction where the consideration actually given or received by the debtor is conspicuously more or less, respectively, than fair market value consideration is a transaction at undervalue.
- The requirement in paragraph 96.1(2)(b) that the trustee establish intent in transactions with arms’ length parties be removed. The fact that a transaction was conspicuously less than fair market value and the debtor was insolvent at the time ought to be sufficient to reverse the transaction.
- The phrase “to defeat the interests of creditors” in subsection 96.1(3) be replaced with “defeat, hinder, delay or defraud creditors,” to be consistent with fraudulent conveyance legislation.
- The BIA provide that making an application under the CCAA is an “initial bankruptcy event.”

Consideration be given to including avoidance provisions in the CCAA parallel to the provisions of the BIA respecting fraudulent conveyances, transactions at undervalue, and payment of dividends and redemptions while the debtor is insolvent.

- **Unpaid Suppliers Rights:** The CBA Section supports the amendments to section 81.1 of the BIA, which will alleviate the problem of suppliers receiving notice of the debtor’s bankruptcy or receivership too late to be able to assert their repossession claim. They also solve the issue of the goods being in the possession of a third party at the time of the bankruptcy or receivership. The CBA Section recommends that consideration be given to a provision in the BIA that would set out the test to be applied where a supplier requests an extension of the 15-day period to recover goods delivered within the 30 days prior to filing.

**Section 243 Receivers:** The CBA Section supports the creation of a “national” receiver. However, it should be clear that an application to appoint a receiver under subsection 243(1) would constitute enforcement of a secured creditor’s security and that the application could not be commenced until after the expiry of the 10-day period referred to in section 244. Further, the section ought to provide a test for the appointment of a receiver. The CBA Section also believes that some guidance should be provided to the Court on its jurisdiction to empower receivers.

Subsection 243(1) should provide that the Court may:

- Direct that a receiver appointed pursuant to subsection 243(1): (i) take possession of the insolvent debtor’s property; (ii) exercise such control over the insolvent debtor’s property or business as the Court considers advisable; (iii) take such other action as the court considers advisable; and
- Grant charges in favour of the receiver to secure: (i) the payment of its fees, and the fees and disbursements of its legal counsel; and (ii) obligations incurred by the receiver in operating the debtor’s business or realizing on the debtor’s assets.

The CBA section further recommends that all of the protections afforded to interim receivers and trustees ought to be afforded to subsection 243(1) trustees. In particular, section 215 ought to be amended to make reference to these receivers.

The CBA Section would also broaden the applicability of section 243. It recommends that not just secured creditors, but “any interested person” be permitted to apply for the appointment of a receiver under subsection 243(1). As well, the definition of “receiver” in section 243(2) should explicitly include receivers appointed under provincial legislation (by removing the words “made under subsection (1)” from paragraph 243(2)(b)).

**Cross-Border Insolvencies:** The CBA Section has supported adoption of the UNCITRAL Model Law of Cross-Border Insolvency (Model Law). However, it believes the ability to commence domestic proceedings could be enhanced by amending the BIA to permit an interim receiver to be appointed where a foreign proceeding has been recognized.

In the case of CCAA proceedings, Bill C-55 would permit the debtor to commence proceedings under the BIA, CCAA, or the *Winding-up and Restructuring Act* (WURA) only after a foreign proceeding has been recognized (proposed subsection 48(4)). This provision should parallel

proposed BIA subsection 271(4). There are also discrepancies between the proposed changes under the CCAA and the BIA on permitting a foreign representative to commence proceedings in Canada. The CBA Section recommends that section 51 of the CCAA permit the foreign representative to commence proceedings under BIA sections 43, 46 to 47.1 and 49 and subsections 50(1) and 50.4(1) as well as under the CCAA.

Last, the CBA Section recommends that it be clear that the cross-border insolvency provisions of the CCAA are available only in respect of a debtor company or a group of debtor companies where the claim against the debtor company or companies exceeds \$5 million and in the context of a foreign reorganization proceeding.

**Critical Suppliers:** The CBA Section generally supports the provisions that enable a court to require a “critical supplier” to continue supplying goods or services to the debtor, and recommends that these provisions be extended to the BIA. The criteria for determining whether a supplier is a “critical supplier” ought to be explicit. The CBA Section also recommends that the provisions specifically require the Court to take steps to ensure that a critical supplier receive adequate assurances of payment, which may include a charge to secure payment.

**Securities’ Firm Bankruptcies:** The CBA Section welcomes the amendment of BIA sections 253 and 261(1) to clarify the status of cash in the accounts of bankrupt securities firms. However, the proposed amendments should go further to clarify that cash in any customer accounts and in any securities accounts of the firm, as well as non-securities accounts of the firm (other than accounts meeting all the requirements of a trust), are to be received by the trustee for distribution. The wording preceding BIA paragraph 261 (2)(a)(ii)(D), namely, “that is held by or for the account of the firm,” should read, “that is held by any person for the account of the securities firm or by or for the account of the firm...”

***International Interests in Mobile Equipment (aircraft equipment) Act:*** The CBA Section recommends additional amendments to ensure that the new CCAA provisions, enabling a party to an agreement, with the reorganizing debtor to terminate that agreement, are consistent with the parallel BIA provisions and include language that restricts the rights of a reorganizing debtor from dealing with leased aircraft objects.

**Estate Solicitors:** The CBA Section agrees there is potential for a conflict of interest between an estate and a secured creditor, where the validity and enforceability of the latter's security is in question. It is essential for the trustee to receive an independent opinion on the secured creditor's security before acting for or assisting that creditor. However, the proposed amendment addressing this issue is too broad and does not address the essential issue relating to the independence of legal counsel. BIA Section 13.4 should require the trustee, prior to acting for or assisting a secured creditor, to obtain an opinion on the validity and enforceability of the secured creditor's security, from legal counsel that has not acted for the secured creditor in any matter involving the bankrupt.

**Five-Year Review:** The CBA Section welcomes further reviews of the BIA and CCAA after Bill C-55 comes into effect, and recommends that the *Winding-up and Restructuring Act* be included in these reviews.

**Enhanced Disclosure:** The CBA Section recommends that the CCAA and BIA require debtors and insolvency practitioners to make "full, true and plain" disclosure in every material document delivered to stakeholders in an insolvency proceeding, and to provide timely disclosure of any material changes in the affairs of the estate under administration. The CCAA and the BIA should require a debtor putting forth a proposal or plan of compromise or arrangement to provide the creditors with an information package similar to that required under provincial securities legislation.

**Role of Monitors:** The CBA Section believes that further clarification is required to ensure that the monitor in CCAA proceedings is perceived as being independent from the debtor and other stakeholders. It recommends that Bill C-55 be amended to: (a) prohibit the monitor from accepting other business engagements with the debtor for a two-year period after the restructuring is complete; (b) prohibit any party who has worked for a stakeholder in relation to the debtor from becoming the monitor; and (c) prohibit the monitor from serving as receiver or interim receiver of the debtor during the reorganization process.

## **Personal Insolvency Summary**

**Return of Property on Discharge:** The CBA Section is concerned about the effect of the amendment requiring that any disclosed property of a bankrupt found incapable of realization be returned to the bankrupt before the trustee's discharge. This could lead to bankrupts disclosing property, but withholding information about value. Therefore, the CBA Section recommends that the bankruptcy trustee be entitled to retain its interest in any property that may be capable of realization in the future, after the trustee's discharge.

**Sale of Assets in a Proposal:** The CBA Section recommends that the restriction on a reorganizing debtor's ability to sell assets outside the ordinary course apply to individual as well as corporate debtors.

**Consumer Proposals:** With the increased complexity in administering estates as a result of increasing in the dollar limit for consumer proposals from \$75,000 to \$250,000, the CBA Section recommends that the fee schedule or tariff applicable to consumer proposals permit the administrator to recover any necessary disbursements for legal fees.

**Reinstatement of Consumer Proposals:** The CBA Section agrees that a new statutory procedure to cure automatic annulments is required. However, the debtor, as well as the administrator, ought to be able to apply to reinstate an annulled consumer proposal after a three-month default.

**Surplus Income:** The CBA Section recommends adopting the Personal Insolvency Task Force (PITF) definition of total income, namely all revenues earned at any time before discharge that have not been received before the date of bankruptcy. Continuing to base revenue on the date of receipt encourages strategic conduct by debtors to defer receipt of income until after discharge.

**Requirements to Pay:** The CBA Section recommends that income from RRSPs and RRIFs be included in the assets subject to a Requirement to Pay. There is no reason to permit enforceability against pension income but not against RRSP or RRIF annuity income, if that

income is sufficient to justify a section 68 obligation. It also recommends that there be more certainty in when a Requirement to Pay terminates, and that a Requirement to Pay terminate after nine months, or upon certification by the trustee that the automatic discharge will take place after 21 months, after 21 months.

**Undervalued Transactions:** The CBA Section fears that the non-arms' length provisions will apply to transfers of family property pursuant to separation agreements or family court orders, despite good faith and lack of knowledge that the transaction was undervalued. It recommends that these transactions be excluded from the application of section 96.1.

**Automatic Discharge:** The CBA Section questions why the BIA amendments would extend the automatic discharge solely on the basis of surplus income during the initial period. The CBA Section recommends a threshold level of surplus income in order to extend the automatic discharge.

**Payments to Creditors on Discharge:** The CBA Section believes that the amendment permitting the court to direct that the bankrupt pay money to any creditor, any class of creditor, to the trustee, or to the trustee and one or more creditors, will result in tactical posturing and secret deals between debtors and creditors. It recommends that the BIA not permit the Court to direct payment to an individual creditor.

**Tax Debtors:** The CBA Section recommends that the amendments relating to discharge hearings for tax debtors apply to all cases where an unsecured creditor is owed more than \$200,000 and the debt represents at least 75% of the total unsecured claims against the bankrupt.

**Section 175:** The CBA Section recommends that BIA section 175 not be repealed. A certificate may give some comfort to a debtor who suffers from the moral stigma of bankruptcy.

**Student Loans:** The CBA Section supports a reduction in the non-dischargeability provision for student loans. However, it recommends that the time for a hardship hearing be reduced further, to one year after ceasing to be a student. Further, the provision should be explicit that a partial discharge of student loans may be granted in connection with the hardship hearing.

**Costs on Bankruptcy Discharge:** The CBA Section recommends that BIA subsection 197(7) provide that a court may award costs in favour of the bankrupt as well as the bankruptcy trustee, where there is a frivolous and vexatious opposition to a discharge.

**Discharge of Section 178 Claims in Proposals:** The CBA Section recommends that the release of a claim under section 178 should be possible only if the creditor votes in favour of a proposal that explicitly provides for the compromise of that claim, to avoid passive acquiescence of a creditor to be taken for assent.

**Senate Recommendations not Included in Bill C-55:** The CBA Section recommends adoption of the Senate Committee recommendations relating to reaffirmation agreements, non-purchase money security interests in exempt property, recognition of cross-border personal insolvency discharges, and family law recommendations relating to addressing technical deficiencies in the 1997 support amendments to the BIA, exempting assets, preventing the bankruptcy trustee from intervening in matrimonial litigation, and creating a bankruptcy remedy against the fraudulent or malicious dissipation or concealment of property to defeat family property claims.

With these suggested modifications, the CBA Section believes the BIA and the CCAA will better reflect the intention behind the various provisions, ensure that they are effective, and will reduce any unintended consequences negatively affecting the rights of debtors and creditors.

# **Submission on Bill C-55 – Bankruptcy Reform**

## **I. INTRODUCTION**

The National Bankruptcy and Insolvency Law Section of the Canadian Bar Association (the CBA Section) is pleased to present this submission to the Standing Committee on Industry, Natural Resources, Science and Technology for consideration in its study of Bill C-55, which amends the *Bankruptcy and Insolvency Act* (the BIA) and the *Companies' Creditors Arrangement Act* (the CCAA), and creates the *Wage Earner Protection Program Act* (the WEPP Act).

The CBA Section has a long history of contributions to government reform initiatives on these subjects. It has, in particular, been involved with the recent amendments arising from the mandated five year review of the BIA and the CCAA, beginning with its submissions to the Senate Standing Committee on Banking, Trade and Commerce. This submission is the culmination of a national consultative process with members of the Section Executive in all parts of Canada and builds on our past submissions on bankruptcy and insolvency reform.

The Family Law Section of the Canadian Bar Association has reviewed this submission, and fully supports the recommendations and commentary regarding family law.

## **II. COMMERCIAL INSOLVENCY**

### **A. Pensions**

#### **BILL C-55**

Bill C-55 will amend the BIA to create a charge (the Pension Charge) over all of the assets of a debtor to secure: (a) unremitted employee pension contributions; (b) unpaid employer contributions in respect of defined contribution pension plans; and (c) unpaid normal costs as

required by the applicable pension legislation in respect of a defined benefit plan (the Unpaid Pension Contributions).

If an insolvency administrator realizes on any assets subject to the Pension Charge, that insolvency administrator will become personally liable for the amounts secured by the Pension Charge up to the amount realized and will be subrogated to any rights that the pension plan might have to recover those amounts.

Bill C-55 will also amend the BIA and the CCAA to require that a proposal or plan provide for the payment in full of amounts subject to the Pension Charge unless an agreement approved by the pension regulator is in place with respect to the payment of any Unpaid Pension Contributions.

### **CBA COMMENTARY**

The CBA Section takes no position with respect to the requirement that plans and proposals provide for the payment in full of any Unpaid Pension Contributions. It is opposed to the creation of the Pension Charge. The CBA Section's February 2005 Submission to Industry Canada (the February 2005 Submission), in the context of a super-priority for wage claims, noted that super-priorities have not proven to be effective and they disadvantage other stakeholders (secured creditors in particular). Its reasons for opposing the Pension Charge are the same.

However, if the Pension Charge is to be created, it must operate effectively. One aspect of Bill C-55 that may hinder its effective operation is omitting fees and disbursements for insolvency administrators. Bill C-55 effectively puts the onus on insolvency administrators to realize upon assets subject to the Pension Charge, and they are personally liable for the gross amount that they recover. However, there is no mechanism for ensuring payment of the fees and disbursements incurred by the insolvency administrators in realizing on assets subject to the Pension Charge.

**RECOMMENDATION:**

1. **The CBA Section recommends that Bill C-55 be amended to provide that the fees and disbursements of insolvency administrators incurred in realizing on assets subject to the Pension Charge be paid out of the realization funds in priority to all other claims.**

**B. Wage Earner Protection**

**BILL C-55**

Bill C-55 proposes a two-prong approach to compensating employees for unpaid wages in insolvency situations:

- (a) Creation of a wage-earner protection program (WEPP) whereby certain employees will be paid any unpaid wages and vacation pay up to \$3,000 in the event of a receivership or bankruptcy. Payment will be made from a fund created out of the Consolidated Revenue Fund to be administered by the Minister of Labour and Housing.
- (b) Creation of a super-priority charge (Employee Charge) on all “current assets” to secure unpaid wages and vacation pay up to a maximum of \$2,000 per employee. Where an employee receives payment under the WEPP, the Minister of Labour will be subrogated to the employees’ claims secured by the Employee Charge.

**CBA COMMENTARY**

**(a) Wage-Earner Protection Program**

The CBA Section supports the creation of the WEPP as an effective means to provide a reasonable measure of wage protection for unpaid employees. The CBA Section does, however, have a number of suggestions to improve the effectiveness of the WEPP.

**Compensation of Insolvency Administrators:** The WEPP Act will impose duties on insolvency administrators, and permit them to charge reasonable fees and disbursements for performing these duties, to be paid out of the debtor’s property (section 22). However, no special priority is created in the BIA for these fees or expenses. As a result, the insolvency administrator’s entitlement to fees for services would be subordinate to the claims of secured creditors.

**RECOMMENDATION:**

2. **The CBA Section recommends that a priority charge be created for the fees and disbursements of insolvency administrators incurred in performing the duties required by the WEPP Act.**

**Criminal Liability of Insolvency Administrators:** The WEPP Act makes it an offense for insolvency administrators to fail to perform their statutory duties. Insolvency administrators may be exposed to liability in circumstances where they are unable to perform their duties under the WEPP Act as a result of defects in the debtor’s records.

**RECOMMENDATION:**

3. **The CBA Section recommends that subsection 38(2) of the WEPP Act be amended to read “Every person who, without reasonable cause, fails to comply with ...”**

**(b) Super-Priority Charge**

In its February 2005 submission, the CBA Section opposed the creation of a super-priority for unpaid wages. The CBA Section continues to believe that a super-priority charge is not an effective means to protect employees. Enhancement of the priority for unpaid employee remuneration through the creation of the Employee Charge will not guarantee payment to the employees. Other statutory super-priority regimes such as the deemed trust for unremitted source deductions have not proven to be effective in terms of enforcement. The Employee Charge will have the effect of placing the burden of unpaid wages and vacation pay on other creditors, particularly secured creditors.

However, if the Employee Charge is to be created, it must be structured to make it as effective as possible and lessen the impact on other creditors. The CBA Section recommends a number of ways to accomplish this goal.

**Definition of Current Assets:** The definition of current assets in Bill C-55 is not sufficiently clear and does not use well-recognized terms. In particular: (a) the term “unrestricted cash” is not sufficiently clear; and (b) the concept of assets expected to be converted into cash or consumed in the production of income within one year or the normal operating cycle of the debtor is likely to lead to disputes.

**RECOMMENDATION:**

- 4. The CBA Section recommends that Bill C-55 be amended to clarify the types of assets to which the Employee Charge attaches by using more clearly defined terms. It may be appropriate to adopt definitions from provincial or territorial personal property security legislation (inventory and receivables, for example) to describe what are current assets.**

**Payment of Fees and Disbursements:** Bill C-55 puts the onus on insolvency administrators to realize upon assets subject to the Employee Charge. They are made personally liable for the gross amount they recover, but there is no mechanism for ensuring that their fees and disbursements incurred in connection with realizing on these assets are paid.

**RECOMMENDATION:**

- 5. The CBA Section recommends that Bill C-55 be amended to provide that the fees and disbursements of insolvency administrators incurred in realizing on assets subject to the Employee Charge be paid out of the realizations in priority to all other claims.**

**Subrogation to Rights Against Directors:** The Employee Charge may result in assets otherwise available to satisfy the claims of other creditors being used to satisfy employee claims. The debtor's directors may also be personally liable to pay these obligations. Where wages are recovered from the debtor's assets subject to the Employee Charge (either by the employees directly or indirectly by receipt of payment from the WEPP which, in turn, recovers from debtor's assets subject to the Employee Charge), the debtor's directors may benefit at the expense of creditors. Bill C-55 does not provide that the estate subrogates to the employees' right to pursue directors when assets are realized pursuant to the Employee Charge.

It is worth noting that the provisions of Bill C-55 with respect to unfounded pension liabilities contemplate subrogation rights for insolvency administrators. Bill C-55 will amend BIA section 136 to give secured creditors whose realizations are reduced as a result of the Employee Charge or the Pension Charge with a preferred claim. They would receive proceeds from the realization of unencumbered assets (which would include any recoveries on subrogated claims) in priority to other creditors, to the extent of the reduction in realizations caused by the Employee Charge.

#### **RECOMMENDATION:**

6. **The CBA Section recommends that an insolvency administrator who pays funds to an employee or the WEPP under the super-priority charge be subrogated to any rights the employee might have against the debtor's directors.**

#### **C. Interim Financing**

##### **BILL C-55**

Bill C-55 will amend the BIA and the CCAA to give the Court specific jurisdiction to make "interim financing" orders. These orders will grant security over a reorganizing debtor's assets in favour of a lender who agrees to lend money to the reorganizing debtor. The Court will have jurisdiction to order that the security granted for interim financing ranks in priority

to the claim of any existing secured creditor. The amount the debtor can borrow will also be in the discretion of the Court and the Court can impose terms on the interim financing.

In considering whether to authorize the interim financing and grant priority security to the interim lender, the Court must consider a number of factors: (a) whether the loan will enhance the debtor's prospects as a going concern; (b) the nature and value of the debtor's assets; and (c) whether any creditor will be materially prejudiced as a result of the debtor's continued operations.

### **CBA COMMENTARY**

The CBA Section generally supports the interim financing provisions. Adding specific provisions to the CCAA to permit interim financing represents a codification of the existing Court practice of approving "debtor-in-possession" or "DIP" financing. The BIA amendments in this regard represent a significant enhancement of the BIA reorganization regime.

The CBA Section finds some of the factors to be considered by the Court in interim financing applications are broad and not directly linked to the appropriateness of allowing the debtor to borrow money for reorganization. Factors such as the confidence of major creditors in the debtor's management are more relevant to the broader question of whether the debtor ought to be, or continue to be, afforded protection under the BIA and the CCAA. In its February 2005 Submission, the CBA Section suggested that the factors to be considered by the Court could be distilled down to a small number of essential factors.

### **RECOMMENDATION:**

- 7. The CBA Section recommends that the factors to be considered by the Court be reduced to:**
  - (a) Whether the proposed financing is necessary to allow the debtor to operate;**
  - (b) Whether the proposed financing will enhance the prospects of the debtor being able to make a viable proposal or plan;**

- (c) The nature and value of the debtor's assets; and
- (d) Whether any creditor will be materially prejudiced by the proposed financing or the security to be provided in connection with it.

## D. Regulators and the CCAA Stay

### BILL C-55

Bill C-55 will amend the CCAA so that the stay of proceedings will prevent regulators from taking steps only in their capacity as creditor and not in their capacity as regulators. The Court will have jurisdiction to stay regulators' actions *qua* regulator, but only on an application brought by the debtor on notice to the regulator.

### CBA COMMENTARY

The CBA Section supports the proposed amendments, which are consistent with our recommendations in the February 2005 Submission.

## E. Collective Agreements

### BILL C-55

Bill C-55 will amend both the BIA and the CCAA to provide that a collective agreement may not be amended except in accordance with the BIA or the CCAA, or the laws of the jurisdiction governing the collective agreement.

The BIA and the CCAA will provide a procedure for a reorganizing debtor to reopen negotiations in a collective agreement, but will not permit the unilateral amendment of the collective agreement. If a reorganizing debtor wants a collective agreement to be amended as part of its reorganization and cannot reach an agreement with the bargaining agent, the debtor can seek an order authorizing the debtor to serve a notice to bargain under the applicable labour relations law. The Court can authorize a notice to bargain where: (a) a viable reorganization cannot be made given the terms of the current collective agreement; (b) the debtor has made good faith efforts to renegotiate the terms of the collective agreement; and (c) failure to make the order is likely to cause irreparable harm to the debtor.

## **CBA COMMENTARY**

The CBA Section was unable to reach a consensus on whether or not the Court ought to have jurisdiction to authorize a reorganizing debtor to unilaterally amend the terms of a collective agreement. The CBA Section agrees, however, that in circumstances where amendments to a collective agreement are necessary for the debtor to reorganize, the ability to serve a notice to bargain will not necessarily resolve the issue.

### **F. Disclaimer of Agreements**

#### **BILL C-55**

Bill C-55 will amend the BIA and the CCAA to permit a debtor to disclaim agreements after the commencement of a reorganization except: (a) eligible financial contracts; (b) collective agreements; (c) financing agreements where the debtor is the borrower; and (d) real and personal property leases where the debtor is the lessor. The disclaimer of real property leases where the debtor is lessee is also exempted from the application of this amendment, because the BIA already contains specific provisions on the disclaimer of real property leases where the debtor is lessee. These provisions are not impacted by Bill C-55.

In response to a notice from the reorganizing debtor, the other party to the agreement being disclaimed can apply to the Court for an order that the agreement cannot be disclaimed. The Court may prohibit the debtor from disclaiming an agreement if the disclaimer, together with the disclaimer of all the other agreements the debtor is disclaiming, is not necessary for the reorganization.

In the case of an agreement where the debtor gives another party use of intellectual property, the BIA and the CCAA will protect their continued use of the intellectual property notwithstanding the disclaimer, so long as the party continues to abide by its obligations for the use of the intellectual property.

The other party to a disclaimed agreement will be able to file a proof of claim in the reorganization for any damages resulting from the disclaimer.

**CBA COMMENTARY**

The CBA Section supports the inclusion of provisions that permit a reorganizing debtor to disclaim agreements. This will codify the existing practice in CCAA reorganizations and enhance the utility of the BIA reorganization regime.

**Standard for Opposing Disclaimer:** The CBA Section believes that the necessity of disclaiming other agreements ought not to be relevant to whether the debtor can disclaim the specific agreement at issue. The criteria for determining whether an agreement can be disclaimed ought to be specific to the particular agreement and balance the interests of the reorganizing debtor and the other party to the agreement.

**RECOMMENDATION:**

8. **The CBA Section recommends that Bill C-55 be amended to provide that the party to an agreement the reorganizing debtor is proposing to disclaim may obtain an order that the agreement may not be disclaimed, by establishing that serious prejudice will result from the disclaimer and that the disclaimer is not necessary for the reorganization to be successful.**

**Intellectual Property Licenses:** Bill C-55 protects licensees of intellectual property in circumstances where the license is disclaimed by the licensor/debtor. Licensees can continue to use the intellectual property notwithstanding the disclaimer so long as they continue to perform their obligations under the license. The CBA Section is concerned that: (a) the right to continue to use licensed intellectual property is absolute; and (b) the proposal is silent on the continuing obligations of the debtor.

The licensee's right to use licensed intellectual property notwithstanding the disclaimer is intended to protect the interests of a licensee whose business may be materially impacted by the disclaimer. The licensee continuing to use the intellectual property may have a negative impact on the debtor/licensor, but the potential serious harm to the licensee mitigates in favour of the continued right to use the intellectual property notwithstanding the disclaimer. However, a balancing of interests should permit the debtor/licensor to establish that the

licensee's business *will not* be adversely impacted by the disclaimer or that it is otherwise appropriate to terminate the licensee's right to use the intellectual property. Further, the debtor/licensor dealing with the licensed intellectual property after a repudiation should not be impeded by any of the terms of the license.

**RECOMMENDATION:**

9. **The CBA Section recommends that section 65.11(5) of the BIA and section 32(5) of the CCAA be amended to: (a) provide the debtor/licensor's disclaimer of an agreement granting an intellectual property license to a licensee does not affect the licensee's right to use the intellectual property unless the debtor establishes that the licensee's business will not be adversely impacted by the disclaimer or that it is otherwise appropriate to terminate the licensee's right to use the intellectual property; and (b) clarify that the debtor/licensor shall have no further obligations under the repudiated license and is not restricted by any terms of the repudiated license.**

**G. Assignment of Agreements**

**Bill C-55**

Bill C-55 will amend the CCAA to permit the Court, on the application of a reorganizing debtor, to order the assignment of agreements other than: (a) eligible financial contracts; (b) collective agreements; and (c) other agreements that are, by their nature, not assignable (personal service contracts, for example).

The BIA will also be amended to permit a reorganizing debtor or an insolvency administrator to assign agreements. In addition to the exclusions in the CCAA, the BIA will exclude real property leases from the category of agreements that can be assigned.

In deciding whether to order an assignment under the BIA or the CCAA, the Court must consider whether: (a) the proposed assignee can perform the debtor's obligations under the agreement; and (b) it is appropriate to assign the agreement to the proposed assignee. In the case of a debtor reorganizing under the BIA, the Court must also consider whether the debtor would be able to reorganize without the assignment.

Under both the BIA and the CCAA, defaults under the agreement to be assigned will have to be cured. Under the BIA, the Court may not order an assignment unless there are no defaults under the agreement. Under the CCAA, the Court must be satisfied there are no financial defaults under the agreement.

### **CBA COMMENTARY**

The CBA Section supports the inclusion of provisions in the BIA and the CCAA that permit the assignment of agreements. The CBA Section notes, however, inconsistencies between the proposed amendments to the BIA and those to the CCAA with respect to: (a) the types of agreements that can be assigned; (b) the test to determine if the debtor can assign an agreement; and (c) the types of defaults that must be cured at the time that the agreement is assigned. There does not appear to be a reason for the difference between the two.

### **RECOMMENDATION:**

- 10. The CBA Section recommends that the BIA provisions for assignment of agreements be amended to parallel the CCAA provisions.**

## **H. Undervalue Transactions**

### **BILL C-55**

Bill C-55 replaces the term “related persons” with “persons not at arms length” to define the class of persons to which an extended twelve month period applies to attack transactions that have an effect of giving them a preference over other creditors.

Bill C-55 replaces the provisions of the BIA dealing with settlements and reviewable transactions with a single provision dealing with “undervalue transactions”. Undervalued transactions will be defined as those where the consideration received by a person is conspicuously less than the fair market value of the assets or services transferred or disposed of in the transaction.

In arms-length undervalue transactions, a remedy will be available where: (a) the transaction occurred up to one year prior to the initial bankruptcy event; (b) the debtor was insolvent when the transaction took place (or was rendered insolvent by the transaction); and (c) the debtor intended to defeat creditors by entering into the transaction.

In the case of non-arms-length undervalue transactions, a remedy will be available where: (a) the transaction occurred up to one year prior to the initial bankruptcy event regardless of the debtor’s financial state or intent; or (b) the transaction occurred up to five years prior to the initial bankruptcy event, where the debtor was insolvent when the transaction took place (or rendered insolvent by the transaction); or intended to defeat creditors.

### **CBA COMMENTARY**

The CBA Section generally supports the collapse of the settlement provisions and the reviewable transactions provisions of the BIA into the single concept of transfers at undervalue. The CBA Section also supports the adoption of “non-arms-length” to expand the class of connected parties subject to a one-year look-back period for attacking transactions.

**Definition of Transaction at Undervalue:** The definition of “transaction at undervalue” may not be sufficiently clear. While the definition appears to include transactions where the debtor either receives conspicuously less or gives conspicuously more than fair market value consideration, use of the term “person” rather than “debtor” may create some confusion. The definition could be made clearer to avoid any disputes on whether it includes transactions where the debtor gives conspicuously more than fair market value consideration.

**RECOMMENDATION:**

11. **The CBA Section recommends that the definition of transaction at undervalue be amended to include any transaction where the consideration actually given or received by the debtor is conspicuously more or less, respectively, than fair market value consideration.**

**Requirement to Prove Intent:** The proposed BIA provisions on transfers at undervalue may not cover some transactions caught by the current BIA provisions on settlements. The current section 91 allows a trustee to reverse the transfer of property for little or no consideration. The trustee need not establish that the transfer was made with any particular intent. Under Bill C-55, a trustee could attack the transaction with an arms' length party only if the debtor was insolvent and intended to defeat interests of creditors at the time of the transfer. The fact that the transaction was at conspicuously less than fair market value and the debtor was insolvent ought to be sufficient to reverse it.

**RECOMMENDATION:**

12. **The CBA Section recommends that Bill C-55 be amended to remove the requirement in paragraph 96.1(2)(b) that the trustee establish intent in transactions with arms' length parties.**

**Use of Terminology:** Bill C-55 uses the term "defeat the interests of creditors" to characterize the requisite intent. This phrase is not the phrase used to describe intent in most provincial and territorial fraudulent conveyances legislation, namely intent to "defeat, hinder, delay or defraud creditors". We fear the Court may conclude that intent to "defeat the interests of creditors" is more specific than "defeat, hinder, delay or defraud." We prefer the latter phrase to ensure consistency with the jurisprudence from fraudulent conveyances cases.

**RECOMMENDATION:**

13. **The CBA Section recommends that BIA subsection 96.1(3) contain the phrase "defeat, hinder, delay or defraud creditors" rather than "defeat the interests of creditors".**

*Companies' Creditors Arrangement Act:* The CCAA does not allow stakeholders to challenge transactions entered into by the reorganizing debtor prior to the commencement of the reorganization. It is now common for creditors in CCAA reorganizations who become aware of a potentially attackable transaction to seek orders lifting the stay of proceedings imposed by the Court at the commencement of the reorganization. These orders are sought so creditors can file a bankruptcy application against the reorganizing debtor, thereby establishing a reference date for attacking transactions if the reorganizing fails. The theory is that if the CCAA reorganization fails and the bankruptcy application proceeds, the trustee can attack earlier transactions than if the creditors applied after the failed CCAA proceeding. The CBA Section believes that creditors should not be required to take active steps in a CCAA reorganization to preserve their ability to attack transactions if the reorganization fails.

**RECOMMENDATION:**

14. **The CBA Section recommends that the BIA be amended to provide that making a CCAA application is an “initial bankruptcy event”, to establish a reference date for attacking transactions under the BIA automatically upon commencement of a CCAA reorganization.**

**The CBA Section also recommends that consideration be given to including avoidance provisions in the CCAA parallel to the BIA provisions for fraudulent conveyances, transactions at undervalue, and the payment of dividends and redemptions while the debtor is insolvent.**

**I. Unpaid Suppliers**

**BILL C-55**

Bill C-55 will amend BIA section 81.1, which confers certain rights to unpaid suppliers. The amended section 81.1 will require a supplier to give notice within 15 days of the bankruptcy

or the appointment of a receiver, to recover goods delivered in the 30 days prior to filing. The notice period may be extended by the insolvency administrator or the Court. Unpaid suppliers may also have access to the remedy if the goods are in the possession of the purchaser's agent or mandatary.

### **CBA COMMENTARY**

The CBA Section supports the amendments to BIA section 81.1. The amendments alleviate two problems:

- suppliers receiving notice of the debtor's bankruptcy or receivership too late to assert their repossession claim; and
- suppliers being unable to recover goods in the possession of a third party at the time of the bankruptcy or receivership.

However, the proposed amendments do not establish a test to be applied when a supplier requests an extension of the 15-day notice period. In the absence of a statutory test, individual insolvency administrators will develop their own “test” to determine when an extension should be granted.

### **RECOMMENDATION:**

15. **The CBA Section recommends that BIA section 81.1 be amended to include a test to be applied where a supplier requests an extension of the 15-day period. The insolvency administrator or the Court must consider: (a) the reason for the failure of the supplier to deliver the notice within the 15-day period; and (b) the prejudice caused by granting the extension.**

## **J. Section 243 Receivers**

### **BILL C-55**

Bill C-55 will amend BIA subsection 243(1) to give the Court jurisdiction to appoint a “national” receiver on the application of a secured creditor.

Bill C-55 also gives the section 243 receiver some of the same protections as trustees and interim receivers against liability for pre-appointment environmental and other liabilities.

The Court will also have the jurisdiction to authorize a section 243 receiver to grant security over the debtor's property in priority to the claims of creditors.

### **CBA COMMENTARY**

The CBA Section supports the creation of a “national” receiver. The proposed amendment should provide a uniform receivership model adapted to current commercial reality and increasing inter-provincial and international transactions. To foster the development of a uniform receivership model, the CBA Section has a number of recommendations.

**Application as Enforcement:** The CBA Section recommends that the amendments make it clear that an application to appoint a receiver under subsection 243(1) would constitute enforcement of a secured creditor's security and that an application under subsection 243(1) could not be commenced until after the 10-day period referred to in section 244.

#### **RECOMMENDATION:**

- 16. The CBA Section recommends that subsection 243(1) be amended so that a secured creditor may not seek the appointment of a receiver before the expiry of the delay in subsection 244(2).**

**Criteria for Appointment:** Subsection 243(1) does not establish a test for the appointment of the “national” receiver. It should outline the circumstances where Court appointment of a receiver would be justified.

#### **RECOMMENDATION:**

- 17. The CBA Section recommends that subsection 243(1) provide that a receiver may be appointed where the Court is satisfied that the appointment is necessary to administer the debtor's assets, or to protect the debtor's estate or the interests of the debtor's stakeholders.**

**Role of the National Receiver:** In the insolvency context, receivers are typically appointed by secured creditors pursuant to provincial or territorial legislation such as the *Courts of*

*Justice Act* (Ontario). The legislation typically says that the Court may appoint a receiver where it is “just or convenient”. The legislation does not give any guidance on the Court’s jurisdiction to grant the receiver powers, to take possession of assets, or deal with other matters relevant to the typical functions of receivers. This is left to the discretion of the Court. While many jurisdictions have developed, or are in the process of developing, “standard” receivership orders, the functions of a receiver may change from province to province. The experience with receivers in Quebec is extremely limited.

The CBA Section believes that subsection 243(1) should be expanded to clarify the jurisdiction of the Court to appoint receivers.

#### **RECOMMENDATION:**

- 18. The CBA Section recommends that BIA subsection 243(1) provide that the Court may:**
- (a) Direct that a receiver appointed pursuant to subsection 243(1): (i) take possession of the insolvent debtor’s property; (ii) exercise such control over the insolvent debtor’s property or business as the Court considers advisable; and (iii) take other action that the Court considers advisable.**
  - (b) Grant charges in favour of the receiver to secure: (i) the payment of its fees, and the fees and disbursements of its legal counsel; and (ii) obligations incurred by the receiver in operating the debtor’s business or realizing on the debtor’s assets.**

**The CBA Section further recommends that the protections for interim receivers and trustees be extended to receivers appointed under BIA subsection 243(1). Specifically, section 215 should be amended to refer to a receiver appointed under subsection 243(1).**

**Who May Apply:** The CBA Section questions why the ability to appoint a receiver under subsection 243(1) is restricted to secured creditors. While secured creditors are typically the stakeholders who seek to appoint receivers and interim receivers, there may be circumstances where it is appropriate for a receiver under subsection 243(1) to be appointed on the application of other stakeholders.

**RECOMMENDATION:**

19. The CBA Section recommends that Bill C-55 be amended to provide that any interested person may apply for the appointment of a receiver under subsection 243(1).

**Definition of Receiver:** The amended definition of “receiver” in subsection 243(2) appears to exclude receivers appointed under provincial or territorial legislation such as the *Courts of Justice Act* (Ontario).

**RECOMMENDATION:**

20. The CBA Section recommends that “made under subsection (1)” be removed from paragraph 243(2)(b).

**K. Cross-Border Insolvency**

**BILL C-55**

Bill C-55 will replace the current cross-border insolvency provisions of the BIA and the CCAA with a modified version of the UNCITRAL Model Law on Cross-Border Insolvency (the Model Law).

**CBA COMMENTARY**

The CBA Section has supported adoption of the Model Law. It is consistent with the pluralist approach to cross-border insolvency endorsed by the Supreme Court of Canada in *Holt Cargo Systems v. ABC Containerline N.V. (Trustee of)*,<sup>1</sup> and embodied in BIA Part XIII and CCAA section 18.6. While the CBA Section would have preferred a more complete adoption of the Model Law, the modifications to the Model Law do not appear to affect the overall approach to cross-border insolvency applicable in Canada.

The CBA Section does, however, have suggestions to improve the proposed cross-border insolvency provisions.

**Ability to Commence Domestic Proceedings:** One cornerstone of the Model Law is the ability of creditors to commence local proceedings to deal with a debtor’s assets in their jurisdiction, even if insolvency proceedings have been commenced in a foreign jurisdiction. While the proposed cross-border insolvency provisions of the BIA and the CCAA will, theoretically, preserve the ability to commence domestic proceedings, the CBA Section recommends some additional measures to substantially improve the process for Canadian creditors.

Under the BIA, the general ability to commence proceedings under the BIA, the CCAA or the *Winding-up and Restructuring Act* (WURA) will be preserved. One of the most effective means of dealing with assets in Canada in connection with a foreign proceeding may be to appoint an interim receiver over those assets without commencing a plenary bankruptcy or insolvency proceeding. An interim receiver would give the Court (and stakeholders) a flexible means of securing control over Canadian assets or operations of a foreign debtor. However, the BIA provisions do not contemplate an interim receiver being appointed in the context of a cross-border insolvency.

Under the CCAA, only *the debtor* could commence proceedings under the BIA, the CCAA or the WURA after a foreign proceeding has been recognized. The CBA Section believes this unduly limits the ability of Canadian stakeholders to take steps to commence proceedings in Canada.

**RECOMMENDATION:**

**21. The CBA Section recommends that:**

- (a) The BIA be amended to permit an interim receiver to be appointed where a foreign proceeding has been recognized.**
- (b) The proposed CCAA subsection 48(4) be amended to parallel the proposed BIA subsection 271(4).**

**Commencement of Proceedings by Foreign Representatives:** Bill C-55 will permit a foreign representative to commence BIA proceedings where debtors can be placed into bankruptcy and an interim receiver or receiver can be appointed. The CCAA, on the other

hand, will only permit the foreign representative to commence CCAA proceedings. This may unduly restrict a foreign representative in recognition proceedings initiated under the CCAA from taking steps to protect Canadian stakeholders. The CCAA should permit the foreign representative to commence proceedings under the BIA as well as the CCAA.

**RECOMMENDATION:**

- 22. The CBA Section recommends that CCAA section 51 permit the foreign representative to commence proceedings under BIA sections 43, 46 to 47.1 and 49 and subsections 50(1) and 50.4(1) as well as under the CCAA.**

**Availability of the CCAA:** The proposed cross-border insolvency provisions could be included only in the BIA (or the CCAA) or incorporated in separate legislation. Bill C-55 includes parallel provisions in the BIA and the CCAA. If cross-border insolvency provisions are included in both the BIA and the CCAA, the Courts may distinguish between the relief afforded in connection with a foreign proceeding under the BIA and the CCAA respectively. With this in mind, the CBA Section believes that the CCAA cross-border insolvency provisions be available only for a debtor company where the CCAA would otherwise apply and in the context of a foreign reorganization proceeding. The CCAA is available only where the claims against the debtor company or a group of debtor companies exceeds \$5 million.

**RECOMMENDATION:**

- 23. The CBA Section recommends that it should be made clear that the cross-border insolvency provisions of the CCAA are available only in respect of a debtor company or a group of debtor companies where the claim against the debtor company or companies exceeds \$5 million and in the context of a foreign reorganization proceeding.**

## L. Critical Suppliers

### BILL C-55

Bill C-55 will amend the CCAA to permit the Court to declare a supplier to be “critical” on the application of a reorganizing debtor. The Court may order that a supplier declared to be critical, supply goods and services to the reorganizing debtor. The Court can order the supplier to provide goods or services on terms consistent with the existing supply relationship or those that the Court considers appropriate.

Where the Court orders a critical supplier to supply goods or services to the debtor, it must give the supplier security over the debtor’s assets to secure payment. The relative priority of this charge is not specified.

### CBA COMMENTARY

The CBA Section generally supports enabling the Court to require that suppliers of goods or services essential to the debtor’s business who cannot be replaced without disruption to the debtor’s business continue to supply goods or services, provided the supplier has adequate assurances of payment.

The CBA Section believes, subject to three recommendations, that the proposed amendment strikes a proper balance between the interests of the debtor (and its various stakeholders) and critical suppliers.

**Meaning of “Critical Supplier”:** Bill C-55 does not define “critical supplier” or provide criteria for determining when it is appropriate to require a supplier to continue to supply goods or services to the reorganization debtor.

### RECOMMENDATION:

24. **The CBA Section recommends that, for a supplier to be considered “critical”, the debtor must establish that the goods or services supplied are essential to its continued business and that the**

**supplier cannot be replaced without causing a disruption to the reorganizing debtor's business.**

**Adequate Assurance of Payment:** Bill C-55 does not go far enough to ensure that a supplier forced to supply goods or services to the reorganizing debtor has sufficient protection for goods or services supplied. The protection of a charge over the debtor's assets is only as good as the realizable value of the assets after taking into account all charges that rank in priority to the charge.

**RECOMMENDATION:**

- 25. The CBA Section recommends that the Court be specifically required to ensure that a critical supplier receives adequate assurances of payment, which may include a charge to secure payment.**

**Inclusion in the BIA:** Bill C-55 does not amend the BIA to deal with critical suppliers. Bill C-55 will significantly enhance the BIA reorganization regime so that, in the future, the BIA will be used in larger, more complex reorganizations. The inability to force critical suppliers to supply goods and services to the reorganizing debtor in proposal proceedings under the BIA is, however, a serious shortcoming in the BIA reorganization regime. There is no reason to not include critical supplier provisions in the BIA.

**RECOMMENDATION:**

- 26. The CBA Section recommends the addition of critical supplier provisions to the BIA.**

**M. Securities Firm Bankruptcies**

**BILL C-55**

Bill C-55 proposes to amend the definition of "customer name securities" in BIA section 253 and to amend BIA subsection 261(1), which clarifies the broad nature of the cash and securities that vest in the trustee on the bankruptcy of a securities firm.

**CBA COMMENTARY**

BIA subsection 261(2)(a)(ii) seems to put a narrower range of “cash” into the customer pool fund for distribution, restricting it to cash in securities accounts, implying that cash in other types of accounts is not in the pool. Clarification is warranted so that cash in any customer account and in any securities account of the firm, as well as in any non-securities accounts of the firm (other than accounts meeting all the requirements of a trust), are included in the pool.

The CBA Section generally supports the proposed amendments to BIA subsection 261(1). However, it recommends that subsection 261(2)(a)(ii) be amended to refer to cash in the same broad sense as the proposed amendments to subsection 261(1): cash held by any person for the account of the securities firm.

**RECOMMENDATION:**

27. The CBA Section recommends that the phrase preceding BIA paragraph 261 (2)(a)(ii)(D), namely, “that is held by or for the account of the firm,” be amended to read, “that is held by any person for the account of the securities firm or by or for the account of the firm...”

**N. *International Interests in Mobile Equipment (aircraft equipment) Act***

**BILL C-55**

Bill C-55 will make further amendments to the BIA and the CCAA that were amended by the *International Interests in Mobile Equipment (aircraft equipment) Act*.<sup>2</sup>

**CBA COMMENTARY**

In its February 2005 Submission, the CBA Section identified technical deficiencies with the *International Interests in Mobile Equipment (aircraft equipment) Act*. The amendments to the

BIA and the CCAA proposed by Bill C-55 adequately address the key deficiencies identified by the CBA Section.

Bill C-55 will include specific provisions in the CCAA to enable parties to agreements with a reorganizing debtor to terminate those agreements. These provisions should restrict the rights of a reorganizing debtor to deal with leased aircraft objects, consistent with the *International Interests in Mobile Equipment (aircraft equipment) Act*.

**RECOMMENDATION:**

- 28. The CBA Section recommends that Bill C-55 be amended to ensure consistency between the CCAA and the BIA on the ability of a party to an agreement with the reorganizing debtor to terminate that agreement, and include language to restrict the rights of a reorganizing debtor from dealing with leased aircraft objects.**

**O. Estate Solicitors**

**BILL C-55**

Bill C-55 will amend the BIA to require that the trustee, prior to acting for or assisting a secured creditor, obtain an opinion on the validity and enforceability of the secured creditor's security from legal counsel who has not acted for the secured creditor in the two previous years and who is not related to the trustee.

**CBA COMMENTARY**

The CBA Section agrees, based on the potential for conflict between the estate and a secured creditor, that the trustee must have an independent opinion on a secured creditor's security before acting for or assisting that creditor. The CBA Section fears, however, that the proposed amendment is too broad and does not deal with the essential issue. The issue ought to be whether legal counsel acted for the secured creditor in connection with any matter involving the bankrupt at any time.

**RECOMMENDATION:**

29. The CBA Section recommends that BIA section 13.4 be amended to require that the trustee, prior to acting for or assisting a secured creditor, obtain an opinion on the validity and enforceability of the secured creditor's security, from legal counsel who has not acted for the secured creditor in any matter involving the bankrupt.

**P. Five-Year Review****BILL C-55**

Bill C-55 will require a review of the BIA and the CCAA five years after the Bill comes into force.

**CBA COMMENTARY**

The CBA Section fully supports the on-going review of Canada's insolvency system. The WURA should be included to ensure that the entire Canadian insolvency system is reviewed.

**RECOMMENDATION:**

30. The CBA Section recommends that the WURA be included in the five-year review.

**Q. The Monitor****BILL C-55**

Bill C-55 will require a monitor under the CCAA to be a licensed bankruptcy trustee and prohibit any trustee with prior relationships with the debtor in the preceding two years from being appointed as monitor except with court approval.

## **CBA COMMENTARY**

**Role of the Monitor:** The monitor plays a pivotal role in the CCAA restructuring process. It not only is empowered to assist the debtor with the restructuring but it functions as the key source of information about the process for the creditors and the Court. Where the monitor has business or professional relationships with the debtor, the perception that the monitor is not independent can negatively impact the restructuring process. The CBA Section believes that further clarification is required to ensure that the monitor is perceived as being independent from the debtor and other stakeholders.

### **RECOMMENDATION:**

31. **The CBA Section recommends that Bill C-55 be amended to: (a) prohibit the monitor from accepting other business engagements with the debtor for two years after the restructuring is complete; (b) prohibit any party who has worked for a stakeholder in relation to the debtor from becoming the monitor; (c) prohibit the monitor from serving as receiver or interim receiver of the debtor during the reorganization process.**

## **R. Enhanced Disclosure in Insolvency Proceedings**

Disclosure is a cornerstone of the proper functioning of an insolvency system. The decisions made by stakeholders are only as good as the information provided to them. Strong disclosure standards promote efficient asset allocation and prevent fraud. Unfortunately, disclosure historically has been a weak link in the insolvency process.

To strengthen disclosure in insolvency proceedings, the CBA Section believes that standards akin to those in the securities regulation field are appropriate. Specifically, restructuring companies, monitors and trustees, interim receivers and receivers should be required to make *timely* disclosure of material changes, and to make *full, true and plain* disclosure whenever they communicate with creditors or file information with the Court.

A further disclosure issue is proxy solicitation for the creditor vote on a restructuring plan or proposal. Unlike the process of soliciting votes in the solvent setting, there is no standard controlling the content of the material used to solicit votes in favour of restructuring plans and proposals.

**RECOMMENDATION:**

- 32. The CBA Section recommends that the CCAA and the BIA require debtors and insolvency practitioners to make “full, true and plain” disclosure in every material document delivered to stakeholders in an insolvency proceeding and provide timely disclosure of any material changes in the affairs of the estate under administration.**

**The CCAA and the BIA should require that, when putting forth a proposal or plan of compromise or arrangement, the debtor must provide the creditors with an information package similar to that required under provincial and territorial securities legislation.**

### **III. PERSONAL BANKRUPTCY**

#### **A. Sale of Assets by Trustee**

##### **BILL C-55**

Bill C-55 will require the bankruptcy trustee to obtain Court approval to sell or dispose of any asset to a related person. The Court must consider the reasonableness of the sale process, the extent of creditor consultation, the effects of the transaction on creditors and others, whether the price is reasonable and fair, whether good faith efforts were made to sell to non-related persons, and whether the price is better than would be received under all other offers actually received.

## **CBA COMMENTARY**

The CBA Section generally agrees with the concept of imposing restrictions on a bankruptcy trustee's ability to sell assets to persons related to the bankrupt. However, some Section members believe that the amendment should not apply to an individual bankrupt's matrimonial home or other family assets. These assets are normally sold to the bankrupt's spouse. In the view of these members, there is insufficient indication of abuse in this area, and the added cost of Court approval is not warranted. Others view the amendment as appropriate even in this context, noting the risk of abuse without Court supervision of such transactions.

The CBA Section was unable to reach consensus on this point.

## **B. Return of Property on Discharge**

### **BILL C-55**

Bill C-55 will amend the BIA to require that any property of a bankrupt listed in the Statement of Affairs or otherwise disclosed to the trustee before the bankrupt's discharge, and found incapable of realization, must be returned to the bankrupt before the trustee's discharge. If there are inspectors, they must approve the return of the property to the bankrupt.

### **CBA COMMENTARY**

The CBA Section is concerned about the potential adverse effect this amendment may have on realizations. The bankrupt may advise the trustee of the *existence* of an asset of indeterminate value, for example, shares in a private company, yet not divulge the *information* necessary to alert the trustee that the shares have value. The proposed amendment would allow the bankrupt to insist on the return of the shares without any obligation to disclose any information on their potential value. The potential problem may be compounded by administrative pressure imposed on trustees to quickly obtain their discharge.

The CBA Section believes that the trustee ought to be able to retain any property that may prove capable of realization in the future, notwithstanding the trustee's discharge.

**RECOMMENDATION:**

33. **The CBA Section recommends that the bankruptcy trustee be entitled to retain its interest in any property, after the trustee's discharge, that may be capable of realization in the future.**

**C. Sale of Assets in a Proposal**

**BILL C-55**

Bill C-55 will amend the BIA to provide that a corporate debtor in a proposal cannot sell or dispose of assets outside the ordinary course of business without Court approval.

**CBA COMMENTARY**

The CBA Section agrees that a reorganizing debtor ought not to be able to sell or dispose of assets out of the ordinary course, but believes that this recommendation should apply to individual as well as corporate debtors.

**RECOMMENDATION:**

34. **The CBA recommends that the restriction on the ability of a reorganizing debtor to sell or dispose of assets out of the ordinary course apply to individual as well as corporate debtors.**

**D. Consumer Proposals**

**BILL C-55**

Bill C-55 will increase the dollar limit for consumer proposals from \$75,000 to \$250,000 or other prescribed amount.

## **CBA COMMENTARY**

The CBA Section agrees that the limit for consumer proposals should rise. The consumer proposal scheme does not permit an administrator to recoup disbursements for legal fees. Administrators are likely to encounter more complex legal issues with the increased dollar value of proposals. They should not suffer reduced fees if they need to retain counsel.

### **RECOMMENDATION:**

- 35. The CBA Section recommends that the fee schedule or tariff applicable to consumer proposals permit the administrator to recover any necessary disbursements for legal fees.**

## **E. Re-Instatement of Consumer Proposal**

### **BILL C-55**

Bill C-55 will amend the BIA to provide for the reinstatement of a consumer proposal after a three-month default. The procedure to reinstate the proposal would require the administrator to send notice of reinstatement to creditors within ten days of the deemed annulment. Creditors have 45 days to object, failing which the proposal is revived. Upon timely objection by a creditor, the administrator may apply to court to revive the proposal.

## **CBA COMMENTARY**

The CBA Section agrees that a new statutory procedure to cure automatic annulments is required. The CBA Section questions whether the 10-day period will provide adequate time for the administrator to react to the deemed annulment in practice. The CBA Section also believes that the debtor, as well as the administrator, ought to be able to apply to revive the consumer proposal.

### **RECOMMENDATION:**

- 36. The CBA Section recommends that the debtor be permitted to apply to reinstate an annulled consumer proposal.**

## **F. RRSPs and RRIFs**

### **BILL C-55**

Bill C-55 will amend the BIA so that, subject to any prescribed conditions and limitations, RRSPs and RRIFs are exempt from distribution except for contributions in the 12 months, or in any longer period that the court may specify, before the date of bankruptcy.

### **CBA COMMENTARY**

The CBA Section supports the proposed RRSP and RRIF exemption, but remains of the view that a two-year mandatory clawback period better achieves the necessary balance between the various conflicting interests. That said, a 12-month period that may be extended by the Court is a significant improvement over a fixed 12-month period.

## **G. Surplus Income**

### **Bill C-55**

Bill C-55 will define total income to include all revenues received while the debtor is bankrupt, including damages for wrongful dismissal, a pay equity settlement, or worker's compensation, but does not include any gift, legacy, inheritance or other windfall.

### **CBA COMMENTARY**

The CBA Section believes that it would be best to adopt the Personal Insolvency Task Force (PITF) recommendation to define total income to include all revenues *earned* at any time before discharge that have not been received before the date of bankruptcy. By basing inclusion of revenue on the date of receipt, strategic conduct by self-employed bankrupts or those employed by friendly parties can defer receipt of income until after discharge.

### **RECOMMENDATION:**

- 36. The CBA Section recommends adoption of the PITF definition of total income, namely all revenues earned at any time before discharge that have not been received before the date of bankruptcy.**

## H. Requirements to Pay

### BILL C-55

Bill C-55 will provide that: (a) a Requirement to Pay under section 68 will be enforceable against the bankrupt's property, including exempt property and GST refunds, but not against RRSPs or RRIFs; and (b) subject to Court order, the Requirement to Pay terminates on the day the bankrupt would be discharged but for a notice of opposition.

### CBA COMMENTARY

**Scope of Assets:** The CBA Section questions why income from RRSPs and RRIFs should be excluded from the assets subject to a Requirement to Pay. There is no reason to permit enforceability against pension income but not against RRSP or RRIF annuity income, if that income is sufficient to justify a section 68 obligation. This would perpetuate the problem of unenforceable section 68 orders where the debtor's income is funded by RRSP or RRIF withdrawals or payments.

#### RECOMMENDATION:

37. **The CBA Section recommends that income from RRSPs and RRIFs be included in assets subject to a Requirement to Pay issued under section 68.**

**Termination:** The CBA Section believes that the language used to describe when a Requirement to Pay terminates is not sufficiently certain. The Requirement to Pay should terminate after nine months or, when the trustee certifies that the automatic discharge has been extended to 21 months, after 21 months.

#### RECOMMENDATION:

38. **The CBA Section recommends that a Requirement to Pay terminate after nine months or, upon certification by the trustee that the automatic discharge will take place after 21 months, after 21 months.**

## I. Undervalued Transactions

### **BILL C-55**

The Bill C-55 provisions on transactions at undervalue are described in the Commercial Insolvency portion of this submission.

### **CBA COMMENTARY**

In addition to the issues raised under Commercial Insolvency, the CBA Section has some concerns about transactions at undervalue in the personal insolvency context.

**Application to Separation Agreements:** The CBA Section has concerns with the application of the undervalue transaction provisions to property transfers under separation agreements. The proposed amendment will make these transfers vulnerable despite good faith and lack of knowledge that they are undervalue. It will risk overturning family property resolutions despite a clear policy trend toward encouraging mediated resolution of family disputes. The proposed standard of review, fair market value of the consideration, is highly subjective in family property cases, and does not assist in determining whether an agreement ought to pass muster. The CBA Section believes that the absence of any reference to the recipient's knowledge, intent, or good faith, is a deep flaw in the proposed test. It proposes that these transactions be excluded from the proposed section 96.1. Provincial and territorial fraudulent conveyance legislation would continue to govern improprieties in this area.

### **RECOMMENDATION:**

- 39. The CBA Section recommends that transfers pursuant to separation agreements and family court orders should be excluded from the proposed section 96.1.**

**Impact on Intact Families:** It has been brought to the CBA Section's attention that the non-arms-length provisions may have an unintended effect on intact families. The proposed BIA section 96.1 may jeopardize payments made to support a debtor's family in the five years before bankruptcy. For example, if a married or common-law debtor gives money to his or her spouse while insolvent, the transferee spouse may become liable to the trustee even if the amounts were

reasonable and for the transferee's consumption. On the other hand, use of the word "may" in section 96.1 makes clear that the judiciary has the power to ensure the remedy is used appropriately. We question whether the impact of this provision upon intact families is an issue of concern, and urge further investigation.

## **J. Automatic Discharge**

### **BILL C-55**

Bill C-55 will amend the BIA to provide, unless the discharge is opposed, an automatic discharge for first-time bankrupts after nine months, unless the bankrupt has been required to make surplus income payments in that period, in which case the period will be 21 months. For second time bankrupts, the time period will be two years or three years if the debtor has been required to make surplus income payments.

### **CBA COMMENTARY**

It appears arbitrary to extend the automatic discharge period, and consequently the surplus income payment period, by another year merely because there was surplus income in the initial time frame. The CBA Section believes some threshold of surplus income should be required to extend the automatic discharge period.

### **RECOMMENDATION:**

- 40. The CBA Section recommends a threshold level of surplus income be required to extend the automatic discharge.**

## **K. Payments to Creditors on Discharge**

### **BILL C-55**

Bill C-55 will amend the BIA to provide that, on a discharge, the Court may direct the bankrupt to pay money to any creditor, any class of creditors, the trustee, or the trustee and one or more creditors.

**CBA COMMENTARY**

This apparently practical amendment allows the Court to violate the fundamental policy goal of equality among unsecured creditors and to circumvent both the trustee's fees and the Superintendent's levy. This amendment may lead to private deals between the bankrupt and an opposing creditor. Creditors with inside knowledge of the bankrupt's affairs will be rewarded for concealing that information from the trustee. Instead, this information may be withheld until the discharge hearing, when objecting creditors could reveal the misconduct and attempt to obtain a direction that payment be made solely to them. This may well distort the discharge process and increase tactical posturing and secret deals.

**RECOMMENDATION:**

41. **The CBA Section recommends that the BIA not permit the Court to direct payment to an individual creditor.**

**L. Tax Debtors****BILL C-55**

Bill C-55 will amend the BIA to provide that a bankrupt whose income tax debt exceeds \$200,000 and represents at least 75% of total unsecured proven claims, must have a discharge hearing. At the hearing, the Court must take into account a specified list of factors, including the bankrupt's circumstances at the time the taxes were incurred, the bankrupt's efforts to pay, whether the bankrupt paid other debts rather than tax, and the financial prospects for the future. A one-year review of any order made on the discharge hearing is available if the debtor can show no reasonable probability of compliance with it.

**CBA COMMENTARY**

The formal effect of this amendment is merely to obviate the need for the Canada Revenue Agency to deliver a notice of opposition to the bankrupt's discharge. Presumably, the intent is to call the Court's attention to these problematic cases in a more specific and directed manner, resulting in sterner treatment of these debtors. The CBA Section questions whether there is any good policy reason to restrict the benefit of this amendment to taxes. In our

view, fairness and consistency suggest that it apply in *any* case where one creditor represents at least 75% of the proven unsecured claims and the total debts exceed \$200,000.

**RECOMMENDATION:**

- 42. The CBA Section recommends that a discharge hearing be required where any unsecured creditor is owed more than \$200,000 and that debt represents at least 75% of the total unsecured claims against the bankrupt, unless the creditor consents in writing to waive the hearing.**

**M. Section 175**

**BILL C-55**

Bill C-55 will repeal section 175, so that a bankrupt cannot seek a certificate that the bankruptcy was caused by misfortune without any misconduct, with the effect that any statutory disqualification on account of bankruptcy ceases upon discharge.

**CBA COMMENTARY**

The CBA Section sees no need to repeal section 175. For those who suffer from the moral stigma of bankruptcy, a certificate may be of some comfort where the bankruptcy resulted from truly external sources such as illness, unemployment or disaster.

**RECOMMENDATION:**

- 43. The CBA Section recommends that BIA section 175 not be repealed.**

**N. Student Loans**

**BILL C-55**

Subsection 178(1)(g) reduces the non-dischargeability provision for student loans from 10 years from ceasing to be a student to seven years. It also shortens the date for the availability of a hardship hearing from 10 years of ceasing to be a student to five years.

**CBA COMMENTARY**

The CBA Section agrees with the direction of this amendment. The CBA Section has previously advocated the PITF position that the non-dischargeability period for student loans be reduced to five years, with the hardship hearing available after one year. The CBA Section acknowledges that any change in this legislation must be accompanied by commensurate changes in the student loan rules. Seven years may be an acceptable compromise between these various factors, provided a hardship hearing is available for the meritorious debtor.

Given the very strict jurisprudence that has evolved in connection with hardship hearings, the CBA Section sees no reason why the hardship hearing should not take place earlier in a proper case, such as circumstances of disability, divorce, or chronic illness. The CBA Section recommends that the hardship hearing be available in a much shorter time frame: within one year after the date of ceasing to be a student.

The CBA Section also urges that the provision make explicit that a partial discharge of student loan may be granted in connection with the hardship hearing.

**RECOMMENDATION:**

- 44. The CBA Section recommends that: (a) a hardship hearing for student debtors be permitted within one year after ceasing to be a student; and (b) partial discharges of student loan debt be permitted at the hardship hearing.**

**O. Costs on Bankruptcy Discharge****BILL C-55**

Bill C-55 will amend the BIA so that if a creditor's opposition to the bankrupt's discharge is frivolous or vexatious, the Court may order the creditor to pay costs to the estate.

## **CBA COMMENTARY**

The CBA Section supports this amendment, but believes that it may not go far enough to guard against frivolous and vexatious oppositions. In an opposed discharge, the bankrupt may also retain counsel and incur costs. Where an opposition is frivolous or vexatious, the bankrupt should be entitled to recover its costs.

### **RECOMMENDATION:**

- 45. The CBA Section recommends that BIA subsection 197(7) provide that the Court may award costs in favour of the bankrupt as well as the bankruptcy trustee.**

## **P. Discharge of Section 178 Claims in Proposals**

### **BILL C-55**

Bill C-55 will amend the BIA so that a proposal does not release the debtor from any section 178 claims unless it explicitly provides for the compromise of the claim and that creditor assents to the proposal.

## **CBA COMMENTARY**

The CBA Section agrees with this amendment, but fears the normal meaning of “assent” may include passive acquiescence.

### **RECOMMENDATION:**

- 46. The CBA Section recommends that the release of a claim under section 178 be possible only if the creditor votes in favour of a proposal that that explicitly provides for the compromise of that claim.**

## **Q. Senate Recommendations not Included in Bill C-55**

A number of the personal insolvency-related recommendations in the Senate Banking Committee report were not included in Bill C-55. The CBA Section believes that some of these should be adopted.

**Reaffirmation Agreements:** The CBA Section supports eliminating implied reaffirmation agreements that can cause serious injustice.

**Non-Purchase Money Security Interests in Exempt Property:** The CBA Section agrees (with reservations on the inclusion of motor vehicles) with the PITF and Senate Banking Committee recommendation to void non-purchase money security interests in exempt personal property. The CBA Section is aware of the abuses in this area in connection with household furniture and appliances, which typically have minimal resale value, and the vulnerability of consumer debtors to coercion. This recommendation would significantly remediate the reaffirmation concern noted elsewhere in the Senate Committee Report.

**International Personal Insolvency:** The PITF and the Senate Committee recommended the creation of a remedy for cross-border personal insolvency to ensure that foreign discharges would be recognized in Canada. The CBA Section agrees.

**Family Law Issues:** In its February 2005 Submission, the Section noted its agreement with the five family law recommendations in the Senate Committee Report. Two of these recommendations address technical deficiencies in the 1997 support amendments to the BIA, which were never intended to impair the enforcement or collection of support. The recommendation that bankruptcy not stay or release any claim for equalization or division of exempt assets comports with judicial policy expressed in reported cases. It eliminates the unnecessary expense and risk that spouses currently face in having to obtain, before the bankrupt's discharge, a court order granting leave to pursue their equalization claim against pensions or other exempt assets. The fourth recommendation fixes a distortion in the case law that permits a bankruptcy trustee to intervene in matrimonial litigation in circumstances that result in substantial injustice. The final recommendation creates a new bankruptcy remedy against fraudulent or malicious dissipation or concealment of property to defeat family property claims.

#### **IV. CONCLUSION**

The CBA Section applauds the creation of the WEPP, which will provide direct and immediate compensation to employees of companies in receivership or bankruptcy. It is truly an idea whose time has come. Its merits have been recognized repeatedly by previous Parliamentary Committees, including the Landry Committee (1981), the Coulter Committee (1986) and the Advisory Council on Adjustment. The CBA Section also appreciates the opportunity to comment on the amendments to the BIA and the CCAA. With the modifications suggested by the CBA Section, we believe the BIA and the CCAA will better reflect the intention behind the various provisions, ensure that they are effective, and will reduce any unintended consequences negatively affecting the rights of debtors and creditors.