

Summary of Key Issues in Chapter 47 of the Statutes of Canada, 2005, and Chapter 36 of the Statutes of Canada, 2007

Both the *Bankruptcy and Insolvency Act* (BIA) and the *Companies' Creditors Arrangement Act* (CCAA) are amended by Chapter 47 of the Statutes of Canada, 2005, and Chapter 36 of the Statutes of Canada, 2007 (c.47 and c.36 respectively). The legislative amendments are broad ranging and significant and are intended to achieve the following main goals:

1. To encourage restructuring of viable businesses as an alternative to bankruptcy. In this regard, the CCAA will be significantly modified to provide increased predictability and consistency while preserving its flexibility.
2. To improve the protection for workers in bankruptcy. The amendments also create the legislative framework for the Wage Earner Protection Program (WEPP), which will ensure that workers receive compensation for their claims.
3. To make the insolvency system fairer and to reduce the potential for abuse. Inequities in the treatment of personal bankruptcies will be addressed and the scope for abuse will be curbed, while respecting the fundamental objective of providing a fresh start to the honest, but unfortunate, debtor.

The following is a summary of key issues that are addressed in c.47 and c.36.

COMMERCIAL ISSUES

Wage Earner Protection Program Act

The *Wage Earner Protection Program Act* creates the Wage Earner Protection Program (WEPP), which provides for the payment of outstanding wages (capped at \$3,000) to individuals whose employment is terminated as a result of a bankruptcy or receivership. The term "wages" is defined to include salary and vacation pay, but does not include severance or termination pay. Employee claims are reduced by any amount paid to them by a receiver or trustee.

The WEPP provisions allow the program to cover insolvency professionals' fees in certain cases and under certain conditions where there are insufficient assets to cover the costs of carrying out those duties related to the operation of the WEPP. Trustees and receivers are required to perform numerous duties to support the operation of the program. A due diligence defence has been included.

Wage Claims

The claims of workers under the WEPP are secured against current assets (cash, accounts

receivable and inventory) to the extent of \$2,000. Division I proposals under the BIA and plans of compromise or arrangement under the CCAA must provide for payment of those claims immediately after court approval/sanction.

Section 138 of the BIA, dealing with the postponement of wage claims of relatives, is repealed and new provisions have been added to preclude persons who were not dealing at arm's length with the bankrupt from having a secured claim for wages unless the trustee/receiver determines it is appropriate in the circumstances. Officers and directors are also precluded from having a secured claim for wages.

BIA s. 2, s. 4(5), s. 60(1.3), s. 81.3, s. 81.4 and CCAA s. 6(5)

Pension Protection

Provisions are added to provide a priority over all assets for the payment of normal pre-filing pension contributions, not including any unfunded pension liabilities, in bankruptcies and receiverships. As well, Division I proposals and CCAA plans that do not provide for these payments are not to be approved by the court unless the parties to the pension plan have entered into an agreement approved by the relevant pension regulator.

BIA s. 60(1.5) & (1.6), s. 81.5 and s. 81.6 and CCAA s. 6

Collective Agreements

Any collective agreement between an employer and a union shall remain in force on its terms unless the agreement is amended by agreement of the parties. Upon application by an insolvent person, the court may make an order authorizing the insolvent person to serve a notice to bargain on the union pursuant to the labour legislation of the relevant jurisdiction. If the court-ordered bargaining fails, there is no provision for the court to disclaim, terminate or revise the collective agreement. If the collective agreement is amended by agreement of the parties, the union has a claim as an unsecured creditor for the value of concessions granted.

BIA s. 65.12 and CCAA s. 33

Liability of Trustees

Trustees and monitors who carry on the business will not be liable for any claims that existed prior to their appointment explicitly, including liability as a "successor employer."

BIA s. 14.06(1.2) & (1.3) and CCAA s. 11.8

Monitors

Monitors under the CCAA must be licensed trustees and the company's auditor may not be the

monitor.

CCAA s. 11.7

Interim Receivers

Time limits regarding the duration of interim receiverships have been established and restrictions have been introduced relating to the powers that may be granted to interim receivers. The application for the appointment of an interim receiver is to be filed in the “locality of the debtor.”

BIA s. 46(4), s. 47(1) & (4) and s. 47.1(4)

National Receivers

Judges exercising their powers under the BIA may appoint receivers under section 243 of the BIA. The term “receiver” also refers to receivers appointed under provincial legislation and explicitly gives the court authority to appoint the receiver to take any action the court considers advisable. Receivers so appointed must be licensed trustees. The application for the appointment of a receiver is to be filed in the “locality of the debtor.”

If a notice to enforce security is to be sent under s. 244(1) of the BIA, the court may not appoint a receiver until the 10-day notice period has expired unless the debtor consents to an earlier enforcement or the court considers it appropriate to appoint a receiver before then.

BIA s. 243

Regulatory Stay

A regulatory body is not stayed in its function except to the extent that it is seeking to enforce rights as a creditor.

BIA s. 69.6 and CCAA s. 11.1

Interim Financing

The court may grant interim financing with priority over existing security interests as the court may specify. An application for interim financing must be made on notice to secured creditors who are likely to be affected by the order.

The factors for the court to consider on an application for interim financing are modified, and it is made explicit that interim financing charges may not secure pre-existing debts.

BIA s. 50.6 and CCAA s. 11.2

Disclaimer and Assignment of Agreements

Disclaimers

Agreements (more commonly referred to as “executory contracts”), other than certain specified agreements, may be disclaimed in a Division I proposal or CCAA case. The co-party may seek a declaration that the disclaimer is invalid and a list of factors is set out for the court to consider in making its determination. If the agreement is disclaimed, the co-party will have a claim for damages as an unsecured creditor. Where the agreement relates to intellectual property, the disclaimer does not affect the co-party’s right to use the intellectual property, nor the right to enforce an exclusive right to use the intellectual property, so long as the co-party continues to perform its obligations under the agreement.

Assignments

Agreements may be assigned, subject to the proposed assignee meeting certain requirements and provided any financial defaults under the agreement are to be remedied. The factors for the court to consider in determining whether to make an order assigning an agreement are specified and include whether the trustee/monitor approved the proposed assignment.

BIA s. 65.11, s. 66(1.1), s. 84.1 and s. 146; CCAA s. 11.3 and s. 32

Asset Sales

The sale of assets in an ordinary administration bankruptcy to “related parties” requires court approval.

In Division I proposals and CCAA cases, assets may not be sold out of the ordinary course of business unless the sale is approved by the court on notice to all secured creditors likely to be affected by the sale. Factors for the court to consider are specified. Where the proposed sale is to a “related party,” the court must be satisfied that additional conditions are met.

BIA s. 30(4), s. 65.13 and CCAA s. 36

Ipsa Facto Clauses

The protection afforded to debtors under consumer proposals and Division I proposals against the impact of “ipso facto” clauses (clauses purporting to entitle the termination of an agreement on the basis of the filing of a proposal) is extended to bankruptcies and CCAA files.

Eligible financial contracts are excluded from the application of these provisions.

BIA s. 65.1 and s. 84.2 and CCAA s. 34

Transfers at Undervalue and Preferences

Transfers at Undervalue

Settlements and reviewable transactions are replaced with a single cause of action — “transfer at undervalue” or “TUV.” It will be a question of fact for the court to determine (1) whether the transfer was at undervalue, and (2) whether the parties were at arm’s length or at non-arm’s length. Persons who are related to each other are deemed not to deal at arm’s length unless there is evidence to the contrary.

If the court finds that the transaction was a transfer at undervalue and that the other party was at arm’s length, the court may grant judgment for the difference between the actual consideration and the fair market value if the transfer took place within one year before the date of the initial bankruptcy event **and** the debtor was insolvent at the time of the transfer **and** the debtor intended to defeat the interests of creditors.

If the court finds that the transaction was a transfer at undervalue and that the other party was not at arm’s length, the court may grant judgment for the difference between the actual consideration and the fair market value if the transfer took place within one year before the date of the initial bankruptcy event or within 1 to 5 years before the date of the initial bankruptcy event if the debtor was insolvent at the time of the transfer **or** intended to defeat the interests of creditors.

Preferences

If the preference was made to a non-arm’s-length creditor within 1 year, no intention test is required. Instead, it is an effects-based test.

The BIA’s transfer at undervalue and preference provisions are incorporated into the CCAA by reference. Trustees and monitors will now have to report on the reasonableness of a decision to exclude the application of the TUV and preference provisions from a proposal or a compromise or arrangement.

BIA s. 2, s. 4(5), s. 50(10)(b), s. 95, s. 96 and s. 101.1 and CCAA s. 23(1)(d.1) and s. 36.1

Directors

The court may order that the director or person acting in such capacity be removed if the court is satisfied that the director may unreasonably impair the insolvent person’s ability to complete a viable proposal/plan. The court may also grant a priority charge against the assets of the insolvent person in favour of the directors for an amount reasonably necessary to indemnify them against obligations and liabilities they may incur following the date of the filing and ending at the completion of the proceeding. The charge may be given priority over existing security. Notice is required to be given to secured creditors who are likely to be affected by the order granting the charge.

BIA s. 64 and s. 64.1 and CCAA s. 11.5 and s. 11.51

Payment of Professional Costs

In Division I proposals and CCAA cases, the court may make an order providing that the property of the debtor is subject to a charge to pay the expenses of professional advisers of any interested party if the court is satisfied that the order is necessary for the effective participation of the interested party. The charge may be given priority over existing security. Notice is required to be given to secured creditors who are likely to be affected by the order.

BIA s. 64.2 and CCAA s. 11.52

Critical Suppliers

In CCAA filings only, the court may make an order declaring a person to be a critical supplier and may make an order requiring continued supply on terms and conditions consistent with the supply relationship or on any basis the court considers appropriate. Critical suppliers must be given security by the court over the property of the debtor and such security may be given priority over any existing security. Notice is required to be given to secured creditors who are likely to be affected by the order.

CCAA s. 11.4

Unpaid Suppliers' Rights

Unpaid suppliers have 15 days after bankruptcy or the appointment of a receiver to submit a written demand for goods delivered to the purchaser or the purchaser's agent (e.g., third-party warehouse) within 30 days before the bankruptcy or appointment of the receiver.

BIA s. 81.1

Shareholder Approval

The amending bill allows the court to order that the constating instrument of the debtor company be amended in accordance with the terms of the proposal or compromise or arrangement. The court may also order the sale of assets outside the ordinary course of business even if shareholder approval was not obtained.

BIA s. 59(4), s. 65.13(1) and CCAA s. 6(2) and s. 36(1)

Plan Approval

The court may establish a claims bar date in respect of voting rights for a plan and for inclusion in a class of creditors for the purpose of any distribution.

CCAA s. 12

Treatment of Equity Claims

Claims arising from the purchase or sale of equity of the bankrupt or debtor company are subordinated to all other claims. The class of creditors having equity claims may not vote at any meeting unless the court orders otherwise. Creditors with equity claims are not entitled to a dividend until all other claims are satisfied. No proposal or compromise or arrangement that provides for payment of an equity claim is to be approved/sanctioned by the court unless all other claims are to be paid in full.

BIA s. 2, s. 54(2)(d), s. 54.1, s. 60(1.7) and s. 140.1 and CCAA s. 2, s. 6(1), s. 6(8) and s. 22.1

Income Trusts

Provisions have been added to deal with the insolvency of an income trust.

BIA s. 2 and CCAA s. 2

Eligible Financial Contracts

The following changes were effected by the *Budget Implementation Act, 2007 (S.C. 2007, c. 29)*

1. Definition of “eligible financial contract” (EFC) is updated and moved to regulations to provide greater flexibility with respect to future updates.
2. Carve out for EFCs from the application of the stay provisions is clarified.
3. Ability of parties to terminate EFCs post insolvency filing (i.e., impact of the ipso facto provision) does not apply to EFCs.

*BIA s. 65.1, s. 84.2, CCAA s. 11.05(1);
Budget Implementation Act, 2007 (S.C. 2007, c. 29) Part 9.*

Aircraft Objects

Provisions have been added regarding the treatment of aircraft objects in Division I proposals and CCAA cases.

BIA s. 65.1(4), s. 69(2)(d), s. 69.1(2)(d) and 69.3(3); CCAA s. 11.07 and s. 34

UNCITRAL

The principles of the UNCITRAL Model Law on Cross-Border Insolvencies are adopted.

BIA s. 267-284 and CCAA s. 44-61

CCAA Oversight

The Office of the Superintendent of Bankruptcy will maintain a public registry of CCAA filings and will have supervisory powers in relation to the conduct of monitors under the CCAA.

CCAA s. 26-31

CCAA Process

Provisions have been introduced with a view to making the process under the CCAA more transparent (i.e., notice provisions, cash-flow statements on a weekly basis, etc.).

CCAA s. 23

CONSUMER ISSUES

Bankrupts with High Income Tax Debt

Bankrupts with personal income tax debt in an amount exceeding \$200,000, representing 75% or more of total unsecured proven claims, will not be eligible for an automatic discharge.

BIA s. 172.1

Surplus Income

First-time bankrupts who have surplus income are required to contribute the surplus to their estate for 21 months and second-time bankrupts are required to contribute for 36 months, subject in both cases to a change in circumstances that impacts on the surplus income obligation.

BIA s. 168.1

Definition of Income

The definition of “total income” has been amended to include amounts received by the bankrupt between the date of bankruptcy and the date of discharge, including amounts for wrongful dismissal, pay equity settlements or workers’ compensation, but not including amounts received during the same time period as a gift, inheritance or other windfall.

A requirement to pay surplus income is enforceable against income that would otherwise be exempt, and income earned but not yet received is included in the definition of “total income.”

BIA s. 68

Income Tax Refunds

Income tax refunds for both the pre- and post-bankruptcy period will form part of the estate of the bankrupt. There is a carve out for the portion of the income tax refund that is garnishable money under a summons for child and spousal support.

BIA s. 67(1)(c)

Post-Discharge Payment Agreements

Agreements regarding the payment of trustee's fees and expenses are permissible and enforceable post-discharge provided: (1) the bankrupt's income is below the level where a surplus income obligation would arise; (2) the amount to be paid under the terms of the agreement does not exceed a prescribed amount; and (3) the payments do not extend beyond 12 months following discharge.

BIA s.156.1

RRSP Exemptions

Amounts held in RRSPs are exempt from seizure in bankruptcy, subject to a possible clawback for contributions made in the 12 months preceding bankruptcy. Where provincial legislation exempts RRSPs from execution, the provincial legislation will apply. Where provincial legislation is silent regarding the treatment of RRSPs, they will be exempt subject to the clawback referred to above.

BIA s. 67(1)

Definition of Consumer Debtor

A consumer proposal may be filed by someone with up to \$250,000 in debts, excluding mortgages on their principal residence.

BIA s. 66.11

Discharge of Second-Time Bankrupts

Second-time bankrupts are eligible for an automatic discharge after 24 months (36 months if they have surplus income).

BIA s. 168.1(b)

Student Loans

The waiting period before which a student loan may be discharged is reduced from 10 years to 7 years. The period before which an application may be made to court to request a discharge on the basis of hardship is reduced from 10 years to 5 years.

The new time frame of 7 years will apply to all those who file for bankruptcy after the coming into force date and to undischarged bankrupts, i.e., student-loan borrowers who have become bankrupt but who have not yet been discharged.

Section 178(1.1) (the “hardship provision”) will be available to all bankrupts, including those who have been discharged prior to the coming into force of the provision.

BIA s. 178

Consumer Proposal Default

Administrators of consumer proposals are given discretion to “revive” a consumer proposal that would otherwise be deemed annulled. Creditors retain the right to object to the revival of the consumer proposal. Courts are given the power to make an order reviving the consumer proposal on any terms the court considers appropriate. An application to court for an order reviving a consumer proposal that has been deemed annulled may be made at any time. The amending bill has extended the time frames in which the administrator of the consumer proposal may send the notices to revive a consumer proposal.

BIA s. 66.31

Inadvertent Discharge of Section 178 Claims

Section 178 claims will not be discharged in a proposal except if the proposal explicitly provides for the compromise of the section 178 claims and the creditor votes in favour of the proposal.

BIA s. 62(2.1) and CCAA s. 19(2)

Debts not Released by Order of Discharge

Debts for services obtained through false pretences or fraudulent misrepresentations, together with debts for property obtained in such circumstances, will be included as undischARGEABLE debts.

BIA s. 178(1)(e) and CCAA s. 19(2)(d)

Collection against Undischarged Bankrupts Where Trustee Discharged

Creditors may realize against the property of a bankrupt without leave of the court if the trustee has been discharged and the bankrupt remains undischarged.

BIA s. 69.3(1.1)

Mandatory Counselling

Debtors making a consumer proposal will have to undergo mandatory counselling in order to receive a certificate of full performance. Bankrupts who have refused to attend mandatory counselling will not be eligible for an automatic discharge.

BIA s. 66.38(2) and 157.1(3)

Statement of Affairs in Proposals

A statement of affairs is required to be completed in all proposals.

BIA s. 50(2)

OTHER ISSUES

Voting Issues / Non-Arm's-Length Voting Rights

If the outcome of a vote at a meeting of creditors is determined by the vote of one or more persons who did not deal with the debtor at arm's length within the 1-year period before bankruptcy, the chair redetermines the outcome not taking the vote of those creditors into account. This then becomes the outcome of the vote unless an application is made to court within 10 days and the court determines another outcome. In an application to revoke or vary a decision regarding the outcome of a vote, the court may suspend the effect of the vote.

BIA s. 109(6) and s. 115.1

Professional Conduct Provisions

Amendments were made to the professional conduct provisions that add clarity to issues that have arisen in various court proceedings.

BIA s. 14.01

Legal Opinion

In order for a trustee of an estate to act for a secured creditor in realizing on its security, the trustee must obtain an opinion that the security is valid from independent legal counsel.

BIA s. 13.4

Orderly Payment of Debts

Provinces that have chosen to “opt in” to the Orderly Payment of Debts provisions may also “opt out.”

BIA s. 242