Legislative Summary **LS-584E**

BILL C-12: AN ACT TO AMEND THE BANKRUPTCY AND INSOLVENCY ACT, THE COMPANIES' CREDITORS ARRANGEMENT ACT, THE WAGE EARNER PROTECTION PROGRAM ACT AND CHAPTER 47 OF THE STATUTES OF CANADA, 2005

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LEGISLATIVE HISTORY OF BILL C-12

HOUSE OF COMMONS

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SENATE

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Legislative history by Michel Bédard

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BILL C-12: AN ACT TO AMEND THE BANKRUPTCY AND INSOLVENCY ACT, THE COMPANIES' CREDITORS ARRANGEMENT ACT, THE WAGE EARNER PROTECTION PROGRAM ACT AND CHAPTER 47 OF THE STATUTES OF CANADA, 2005*

BACKGROUND

Bill C-12, An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and Chapter 47 of the Statutes of Canada, 2005, makes a series of important amendments to federal bankruptcy and insolvency legislation. Bill C-12 has been described as a "technical" bill that is intended to correct some of the formal deficiencies in existing legislation. However, many of the changes it makes are of a substantive nature.

Bill C-12 has a somewhat complicated history. On 3 June 2005, the Government introduced a package of major amendments to bankruptcy legislation in Bill C-55, An Act to Establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts. This bill was tabled following a comprehensive government-led review(1) of the

* Notice: For clarity of exposition, the legislative proposals set out in the bill described in this Legislative Summary are stated as if they had already been adopted or were in force. It is important to note, however, that bills may be amended during their consideration by the House of Commons and Senate, and have no force or effect unless and until they are passed by both houses of Parliament, receive Royal Assent, and come into force.

(1) Amendments made to the *Bankruptcy and Insolvency Act* in 1997 required the federal government to report to Parliament on the operation of the Act within five years. The Government organized regional meetings to obtain feedback from stakeholders about the operation of the *Bankruptcy and Insolvency Act* (BIA) and the *Companies' Creditors Arrangement Act*, and commissioned academics to prepare research reports on various features of the BIA. In 2000, the Superintendent of Bankruptcy established a Personal Insolvency Task Force (PITF) to report on the operation of consumer aspects of the federal bankruptcy legislation and to make recommendations for change. The PITF held meetings over a 15-month period and issued its report in August 2002. In a parallel process, Industry Canada also reported to Parliament in September 2002 on the operation of federal bankruptcy legislation. The role of reviewing these reports and holding hearings on the operation of Canada's insolvency system was assigned to the Senate Standing Committee on Bankruptcy, Trade and Commerce. The Committee issued its report in November 2003.

Bankruptcy and Insolvency Act(2) (BIA) and the *Companies' Creditors Arrangement Act*(3) (CCAA).

Bill C-55 made its way through the parliamentary process on an expedited basis, and received Royal Assent on 25 November 2005, shortly before the minority Liberal government fell. Since the bill was rushed through Parliament, the Senate Standing Committee on Banking, Trade and Commerce requested and received the Government's assurance that it would not be proclaimed in force prior to its referral to that Committee for further study, or before 30 June 2006.(4) To date, Bill C-55 (now Chapter 47 of the Statutes of Canada, 2005) has not been proclaimed into force.

Among other things, Chapter 47 would establish a Wage Earner Protection Program, financed out of the Consolidated Revenue Fund, to provide workers with quick payment of unpaid wages in the event of their employer's bankruptcy or receivership. Indeed, Chapter 47 is perhaps best known for its proposed wage-earner protection scheme. However, it would also make a number of significant amendments relating to commercial and consumer insolvency more generally. In May 2006, the Government indicated that it had not proclaimed Chapter 47 in force because of the numerous technical defects in the legislation resulting from its expedited passage through Parliament, and that an interdepartmental committee was working to address these problems.(5)

On 8 December 2006, in the 1st Session of the 39th Parliament, the Minister of Labour (the Honourable Jean-Pierre Blackburn) tabled a notice of ways and means motion to amend the *Bankruptcy and Insolvency Act*, the *Wage Earner Protection Program Act*

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(2) R.S.C. 1985, c. B-3.

(3) R.S.C. 1985, c. C-36.

(4) Office of the Superintendent of Bankruptcy, "Bill C-55 Receives Royal Assent: Next Steps," http://www.ic.gc.ca/epic/site/bsf-osb.nsf/print-en/br01561e.html (accessed 21 November 2007).

(5) Statements of the Honourable Jean-Pierre Blackburn, Minister of Labour, *House of Commons Debates*, Vol. 131, No. 30, 1st Session, 39th Parliament, 31 May 2006, p. 1500. With regards to the Government's position that Chapter 47 requires modifications, see also the Office of the Superintendent of Bankruptcy, note 4.

According to Mr. Colin Carrie, M.P., Parliamentary Secretary to the Minister of Industry, Bill C-12 was drafted following extensive consultations with a panel of leading insolvency law experts, including practitioners and academics. This panel helped the Department in identifying the technical flaws of Chapter 47 and crafting solutions to these problems. Departmental officials also received input from a wide variety of stakeholders, including the Canadian Bar Association, the Canadian Life and Health Insurance Association and family law advocates. *Speaking Notes for Mr. Colin Carrie, M.P., to the Standing Senate Committee on Banking, Trade and Commerce*, *on Bill C-12: An Act to Amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and Chapter 47 of the Statues of Canada, 2005*, 29 November 2007.

and Chapter 47 of the Statutes of Canada. The Government wanted to "fast track" the proposed bill through the House without amendments. However, before the bill was tabled, the Bloc Québécois requested amendments dealing with the seizure of Registered Retirement Savings Plans (RRSPs) and Registered Retirement Income Funds (RRIFs) in bankruptcy. These amendments were sought on the basis that the provisions of Chapter 47 encroached on Quebec's legislative jurisdiction to regulate RRSPs and RRIFs.(6) The federal government at first refused to make the amendments, and the bill was never tabled. Some six months later, after the Quebec National Assembly passed a resolution urging the federal government to make the amendments,(7) the Government agreed to include the amendments in the bill. On 12 June 2007, the Minister of Labour tabled a new notice of ways and means motion to amend the *Bankruptcy and Insolvency Act*, the *Companies' Creditors Arrangement Act*, the *Wage Earner Protection Program Act* and Chapter 47 of the Statutes of Canada, 2005. Bill C-62, An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and Chapter 47 of the Statutes of Canada, 2005 was tabled on 13 June 2007, and on the following day it was deemed to have moved through all stages and to have been passed by the House.

Bill C-62 died on the *Order Paper* when Parliament was prorogued on 14 September 2007. However, it was reintroduced in the 2nd Session of the 39th Parliament as Bill C-12, An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and Chapter 47 of the Statutes of Canada, 2005. Pursuant to an order of the Speaker made 25 October 2007, Bill C-12 was deemed adopted at all stages and passed by the House on 29 October 2007. It was referred to the Standing Senate Committee on Banking, Trade and Commerce on 15 November 2007.

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(6) See, for example, the debates on this issue in the *House of Commons Debates*, Vol. 141, No. 166, 1st Session, 39th Parliament, 7 June 2007, pp. 1435-1440.

(7) On 7 June 2007, the National Assembly of Quebec passed the following resolution: "That the National Assembly require the Government of Canada to amend the its bill amending *the Bankruptcy and Insolvency Act*, the *Companies' Creditors Arrangement Act*, the *Wage Earner Protection Program Act* and Chapter 47 of the Statutes of Canada (2005), so that it fully respects Québec legislation, namely the provisions of the *Civil Code of Québec* and of the *Code of Civil Procedure*, concerning the immunity from seizure of RRSPs and RRIFs, as well as Québec's jurisdiction in this matter." (*Votes and Proceedings of the Assembly*, 1st Session, 38th Legislature, No. 17, 7 June 2007, p. 138.)

The Committee, chaired by Senator David Angus, conducted hearings on Bill C-12 on 29 November and 5 December 2007. The Minster of Labour (the Hon. Jean-Pierre Blackburn) and the Parliamentary Secretary to the Minister of Industry (Colin Carrie, MP) appeared before the Committee. The Committee also heard from representatives of the Canadian Association of Insolvency and Restructuring Professionals. On 13 December 2007, the Committee conducted a clause-by-clause analysis of the bill and reported back to the Senate. Although the Committee did not recommend any amendments, it submitted formal observations on Bill C-12 along with its report (*Observations to the Fifth Report of the Standing Senate Committee on Banking, Trade and Commerce*). In this document, the Committee indicated that it was reporting back to the Senate without having conducted a comprehensive study and review of Bill C-12 in order to speed up the implementation of wage-earner protection legislation. It wrote:

> As the Committee noted in our Seventeenth Report in the 38th Parliament [on Bill C-55], we unanimously support and approve of wage earner protection for workers of bankrupt employers. In our November 2005 report, we indicated that enhanced protection for these vulnerable creditors was long overdue. More than two years later, we continue to believe that the need is urgent.

However, the Committee acknowledged that some stakeholders had certain reservations about Bill C-12, as well as other aspects of bankruptcy and insolvency legislation more generally. Referring to the Minister of Labour’s statement before the Committee that further amendments to bankruptcy and insolvency legislation could be made in 2008, the Committee expressed its intention to continue studying the legislation, for the purpose of formulating recommendations to the Government. It also indicated that it would be hearing from stakeholders beginning in early 2008.

Bill C-12 received third reading in the Senate on 13 December 2007. On 14 December 2007, it received Royal Assent, and became Chapter 36 of the Statutes of Canada, 2007.

DESCRIPTION AND ANALYSIS

Bill C-12 makes amendments to provisions of the BIA and CCAA, as enacted by Chapter 47, as well as to existing provisions of these Acts. It also makes amendments to Chapter 47, and to the *Wage Earner Protection Program Act*, which will be enacted by Chapter 47 if the latter is proclaimed in force. The amendments made by Bill C-12 can be grouped into three major subject areas: commercial insolvency issues; consumer insolvency issues; and procedural and administrative issues.

A. Commercial Insolvency Issues

1. Protection of Wages

a. *Wage Earner Protection Program Act* (Bill C-12, Clauses 83-94)

Under Chapter 47, a Wage Earner Protection Program is established pursuant to a new Act, the *Wage Earner Protection Program Act* (WEPPA). The WEPPA provides for compensation to employees for unpaid wages and vacation pay earned in the six months immediately before the bankruptcy or the first day on which there was a receiver in relation to the former employer, less any applicable provincial or federal deductions, to a maximum of $3,000 or four times the maximum weekly insurable earnings under the *Employment Insurance Act,* whichever is greater. The WEPPA does not cover claims for severance or termination pay. Compensation is paid out of the Consolidated Revenue Fund. To the extent of the payment made to the employee, the Crown is subrogated to any rights the employee has against the bankrupt employer and any directors of the corporation.

In order to be entitled to make a claim, a person must have been employed by the employer for at least three months. A person cannot make a claim in respect of wages earned during any period in which he or she was an officer or director, had a controlling interest, or occupied a managerial position with the former employer.

Bill C-12 makes the following noteworthy changes to the WEPPA:

- It removes the requirement that the claimant must have worked for the employer for at least three months prior to the date of bankruptcy or receivership (clause 85, section 6 of the WEPPA).

- It clarifies that a person is not eligible to make a claim in respect of wages earned during any period in which the person was an officer or director, had a controlling interest (within the meaning of the regulations), or occupied a managerial position (within the meaning of the regulations) with the former employer. Furthermore, a person is not eligible to make a claim for wages in respect of a period during which he or she was not dealing at "arm's length" with an officer, director, or a person who occupied a managerial position or who had a controlling interest in the former employer (clause 85, section 6 of the WEPPA). Persons who are related to each other are generally deemed not to be dealing with each other at arm's length; however, for the purposes of this section of the WEPPA, a person is considered to deal at arm's length with a related person if the Minister is satisfied that, having regard to the circumstances (including the terms and conditions of the person's employment, his or her remuneration and the duration, nature and importance of work performed), it is reasonable to conclude that the person would have entered into a substantially similar contract of employment if the parties had been dealing with each other at arm's length (clause 83, section 2(5)(a) of the WEPPA).

- Bill C-12 also provides that a claim may be made for unpaid wages and vacation pay earned in the six months immediately before the date of bankruptcy or receivership, *less any amount provided by regulation*. (The WEPPA currently provides that a claim may be made for unpaid wages and vacation pay earned in the six months immediately before the date of bankruptcy or receivership, *less any applicable federal or provincial deductions*). Bill C-12 further clarifies that in the case of an employer who is bankrupt *and* subject to a receivership, the amount due under the WEPPA is the greater of the amount determined in respect of the bankruptcy and the amount determined in respect of the receivership. (Clause 86(1), section 7(1) of the WEPPA.)

- The maximum amount that may be paid out under the WEPPA is capped at the greater of $3,000 and an amount equal to four times the maximum weekly insurable earnings under the *Employment Insurance Act*, *less any amount provided by regulation* (The WEPPA currently provides that the maximum payment is *less any applicable federal or provincial deductions*). See clause 86(2), section 7(2) of the WEPPA.

- Under the WEPPA, the fees or expenses of the trustee or receiver are to be paid out of the estate of the bankrupt or the property of the insolvent employer (whichever is applicable). Bill C-12 adds a new subsection 22(2) to the WEPPA to authorize the Minister to pay the trustee or receiver's fees and expenses, in the circumstances prescribed by regulation (clause 89).

- Bill C-12 adds new provisions to the WEPPA to require any person – other than a person dealing at arm's length with, and providing payroll services to, the employer – to provide information about unpaid wages that are due to the trustee or receiver upon their request. Those dealing at arm's length with, and providing payroll services to, a bankrupt or insolvent

employer, must provide a description of the information that they do not have access to, an estimate of the cost of providing the information that they have, and an estimate of the cost of providing the information that only they have access to. It is an offence to fail to comply with these new requirements, unless the person establishes that he or she exercised due diligence to prevent the commission of the offence (clause 89, sections 21(3)-(4) of the WEPPA; and clause 93, sections 38(2) and (4) of the WEPPA).

- Bill C-12 introduces a due diligence defence for trustees and receivers who are charged with the offence of failure to comply with their duties under the WEPPA (clause 93, section 38(4) of the WEPPA).
- Bill C-12 reduces from six to two years the time limit for instituting a prosecution for an offence under the WEPPA (clause 93, section 39(2)).

b. Limited "Super-Priority" for Wages (Clause 38)

1) Chapter 47

Chapter 47 amends the BIA to provide for a limited "super-priority" (above secured creditors) over bankrupt and insolvent employers' "current assets," for unpaid wages, salaries, commissions or compensation for services rendered in the six months before bankruptcy or the appointment of a receiver, up to a maximum of $2,000. The term "current assets" is defined under Chapter 47 to include unrestricted cash, as well as any other asset that, in the normal course of operations, is expected to be converted into cash or consumed in the production of income within one year (or within the normal operating cycle if longer than one year).

The super-priority over current assets ranks above secured creditors but below the rights of unpaid suppliers to repossess goods and the claims of farmers, fishermen and aquaculturalists in respect of unpaid products supplied to the bankrupt or insolvent employer. In the case of bankruptcy (but not receivership), the super-priority also ranks behind unremitted income tax, employment insurance and Canada Pension Plan deductions deemed to be held in trust under section 67(3) of the BIA.

The super-priority may be acted upon by the Government in exercising the rights of the employee in the bankruptcy proceeding (where payment is made to employees out of the Wage Earner Protection Program) or by individuals who do not qualify for payment under the Program and who can pursue wage claims directly in the bankruptcy process. If there are insufficient current assets to satisfy the wage claims under the limited super priority, any amount

outstanding, up to the maximum of $2,000, may be claimed through the existing preferred creditor status under section 136 of the BIA.(8)

If the trustee or receiver disposes of the current assets covered by the security, it is liable for the claim to the extent of the amount realized on that disposition of assets.

2) Bill C-12

Under Chapter 47, the new super-priority for unpaid wages is secured over the "current assets" of the employer. Bill C-12 redefines the term "current assets" as "cash, cash equivalents – including negotiable instruments and demand deposits – inventory or accounts receivable, or the proceeds from any dealing with those assets" (clause 1(3), section 2 of the BIA).

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(8) Currently under the BIA, creditors are classified as follows: secured creditors, preferred creditors, ordinary creditors and deferred creditors. These classifications determine where creditors rank in relation to their claims against the bankrupt debtor's assets. Secured creditors rank first because a trustee in bankruptcy takes title to a debtor's property subject to the rights of secured creditors in that property. For example, a mortgagee would have first claim on real estate for the unpaid value of a mortgage before any other unpaid creditors could make a claim against that asset.

After secured creditors come the claims of preferred creditors, ordinary creditors and deferred creditors, in that order. Preferred creditor claims must be satisfied before those of ordinary creditors, and claims of ordinary creditors must be dealt with before deferred creditors are entitled to share in the bankrupt debtor's assets. The BIA also ranks claims within the class of preferred creditors, with each sub-class of preferred creditor having priority over the subsequent sub-class. Section 136(1) of the BIA establishes the following order for preferred claims:

a) testamentary and funeral expenses of a deceased bankrupt;

b) fees and expenses of the trustee in bankruptcy and legal costs;

c) the Superintendent of Bankruptcy's levy;

d) unpaid wages and salaries of employees earned within six months prior to the employer's bankruptcy up to a maximum of $2,000, and salespersons' disbursements of up to $1,000 during that six-month period;

e) alimony and maintenance payments accruing in the year prior to bankruptcy;

f) municipal taxes;

g) landlords' claims for up to three months' arrears in rent;

h) certain fees and expenses incurred by execution creditors before a bankruptcy; and

i) claims resulting from employee injuries.

Thus, unpaid wages to a maximum of $2,000 and salespersons' expenses up to $1,000 currently rank fourth among preferred creditors behind funeral expenses, bankruptcy trustee fees and the levy charged by the Superintendent of Bankruptcy. (Margaret Smith, *Protecting Employee Wages in Bankruptcy*, PRB 01-34E, Parliamentary Information and Research Service, Library of Parliament, Ottawa, 6 March 2002, pp. 2-3.)

Chapter 47 provides that the super-priority secures remuneration in respect of services rendered during the six months prior to an employer becoming bankrupt or a receiver being appointed in respect of the employer. Bill C-12 amends this slightly to provide that the charge secures remuneration owing for the period beginning on the date that is *six months prior to the date of the initial bankruptcy event and ending on the date of bankruptcy*. The charge attaches to current assets existing on the date of bankruptcy (clause 38, sections 81.3(1) and 81.4(1)). The main effect of this amendment, when combined with the definition of "date of initial bankruptcy event,"[9] is to provide extended coverage for employees in the event of a failed reorganization attempt by the debtor.[10]

Moreover, Bill C-12 clarifies that the employees can recover the $2,000 secured by the super-priority status either through payment by the trustee or receiver of the remuneration owing to the employee or by the enforcement of the super-priority. In other words, the maximum amount of the charge is $2,000, less any amount paid to the employee by the bankruptcy trustee or receiver (clause 38, section 81.3(1) and 81.4(1)). This amendment covers situations where the trustee or receiver retains the debtor's employees after the bankruptcy or receivership. In such cases, the trustee or receiver frequently agrees to pay the employee remuneration owing for the period prior to the bankruptcy or the appointment of the receiver. The proposed amendments ensure that, in these situations, employees do not receive payment from the trustee and also make a claim under the super-priority.[11]

Bill C-12 also amends the BIA to provide that the super-priority security does not apply to unpaid wage claims of directors and officers of the employer. In addition, it provides that the super-priority does not apply to the unpaid wage claim of any person who did not deal at "arm's length" with the employer – unless, in the opinion of the trustee or receiver,

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(9) Under section 2 of the BIA, the "date of the initial bankruptcy event" refers to the earliest of the following events: the filing of a proposal or a notice of intention (i.e., the commencement of reorganization proceedings); an assignment in bankruptcy; the first application for a bankruptcy order against the person (as defined); or an application in respect of which a bankruptcy order is made. Note that clause 1(6) of Bill C-12 expands the definition of "date of the initial bankruptcy event" in the BIA to include reorganization proceedings under the *Companies' Creditors Arrangement Act* (CCAA). Thus, the "date of the initial bankruptcy event" will include the commencement of reorganization proceedings under either the BIA or the CCAA.

(10) E. Patrick Shea, "The Insolvency Reform Act 2007 – A Review of the Proposed Commercial Insolvency-related Amendments to the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act," *Bankruptcy and Insolvency Law Newsletters*, Houlden and Morawitz Online Newsletter, 27 March 2007.

(11) Ibid.

it is reasonable to conclude that, having regard to the circumstances, the parties would have entered into a substantially similar transaction had they been dealing with each other at arm's length. (Clause 38, sections 81.3(6)-(7) and 81.4(6)-(7) of the BIA).

Finally, Bill C-12 makes the super-priority security applicable on the appointment of an interim receiver as well as of a conventional receiver (clause 38, sections 81.3(9) and 81.4(9) of the BIA).

c. Employment-related Claims of Relatives (Clauses 47-48)

Section 137(2) of the BIA subordinates the claims of a bankrupt's current or former spouse or common-law partner for employment-related remuneration. Section 138 prohibits certain relatives of a bankrupt from claiming a preference under section 136 of the BIA for employment-related remuneration. Bill C-12 repeals these provisions.

2. Amendments to the BIA and CCAA

a. Income Trusts (Clauses 1(3) and 61(2)-(3))

Chapter 47 amends the BIA and the CCAA so that an income trust may undergo insolvency proceedings. It defines the term "income trust" as a trust that has assets in Canada, the units of which are traded in a prescribed stock exchange.

Bill C-12 expands the definition of "income trust" to cover any trust with assets in Canada, if it is structured in one of the following ways:

- its units are listed on a prescribed stock exchange on the date of the initial bankruptcy event; or
- the majority of its units are *held by a trust* whose units are listed on a prescribed stock exchange on the date of the initial bankruptcy event (commonly referred to as a "trust on trust" structure) (clause 1(3), section 2 BIA; and clause 61(2), section 2(1) CCAA).[12]

This amendment ensures that both levels of a "trust on trust" structure – a structure commonly used by many income trusts – may undergo proceedings under the BIA and CCAA.[13]

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(12) Also note that Chapter 47 amends the BIA to include an income trust within the definition of the term "person" (clause 2(3), section 2 BIA). However, under Bill C-12, an income trust is included in the definition of a "corporation," rather than of a "person." This change is not significant, as the term "person" is defined to include a corporation (clauses 1(1)-(2), section 2 BIA).

(13) Blake, Cassels and Graydon LLP, "Proposed Insolvency Law Amendments – Take Two," *Bulletin on Restructuring and Insolvency*, January 2007.

Bill C-12 further clarifies that the term "director," in the case of a trust, means a person occupying the position of trustee, regardless of what the position is called (clause 1(3), section 2 BIA; and clause 61(2), section 2(1) CCAA).

b. Effect of Stay of Proceedings on Regulatory Bodies (Clauses 34-35, 37 and 65)

The CCAA gives provincial and territorial superior courts the power to stay any action, suit or proceeding brought against a company when the company becomes subject to a CCAA order (section 11). This stay of proceedings has been held to apply to provincial market regulators, such as securities commissions or stock exchanges.(14) Such a stay prevents the regulator from being able to take action against a company that is conducting itself inappropriately.(15)

Chapter 47 inserts a new section into the CCAA (section 11.1) to clarify the impact of a stay on a regulatory body. The term "regulatory body" is defined as any person or body having powers, duties or functions relating to the enforcement or administration of a federal or provincial Act, including any prescribed regulatory body (section 11.1(5)). Section 11.1(1) provides that a stay order does not affect the right of a regulatory body with respect to any investigation, suit or proceeding it is taking against the company – except when the regulatory body is seeking to enforce any of its rights as a secured or unsecured creditor. In case of dispute, the company may apply to the court for a declaration as to whether a regulatory body is seeking to enforce its rights as a creditor. Furthermore, on the application of the company, the court may make an order that the regulatory body is not exempted from a stay of proceedings, provided certain conditions are met (sections 11.1(2)-(4)).

Bill C-12 makes some changes to the language of these provisions (at clause 65). For instance, it provides that the regulatory body may not seek "the enforcement of a payment ordered by the regulatory body or the court" (amending the language under Chapter 47, which provides that the regulatory body may not seek "the enforcement of any of its rights as a secured or unsecured creditor").

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(14) Senate, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act*, Report of the Standing Senate Committee on Banking, Trade and Commerce, November 2003, p. 126.

(15) Industry Canada, Marketplace Framework Policy Branch, Policy Sector, *Report on the Operation and Administration of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act*, September 2002, p. 51.

More importantly, Bill C-12 adds parallel provisions into the BIA (section 69.6), in order to ensure that a stay of proceedings under the BIA[16] does not generally prevent regulatory bodies from performing their duties. See clauses 34, 35 and 37 of Bill C-12.

c. Interim Financing (Clauses 18 and 65)

Interim financing, also known as debtor-in-possession financing (DIP financing) is a tool that was first developed in the United States. In DIP financing, a new lender provides an infusion of cash to a business that is seeking reorganization, and in exchange for doing so jumps ahead of other secured creditors.[17] This facilitates the continuation of the debtor company as a going concern pending negotiations for reorganization. DIP financing compromises the claims of other creditors; however, they may benefit if there is a reasonable prospect of a viable restructuring plan.[18]

Neither the BIA nor the CCAA currently contains any provisions on DIP financing. Nonetheless, DIP financing has been authorized by Canadian courts using their "inherent and equitable" jurisdiction in CCAA proceedings.[19]

Chapter 47 introduces new provisions into the BIA and CCAA to specifically authorize court orders for interim financing in reorganization proceedings. New section 50.6 of the BIA and new section 11.2 of the CCAA permit a debtor undergoing reorganization to apply to the court for an order declaring that the debtor's property is subject to a security or charge in favour of any person specified in the order who agrees to lend to the debtor an amount that is approved by the court as being required by the debtor, having regard to the debtor's cash-flow statement. An order for interim financing may be made on any conditions that the court considers appropriate. The interim financing may be provided for a period of 30 days after the commencement of reorganization proceedings,[20] or, if notice of the application has been given

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(16) Under the BIA, where a debtor files a proposal or a notice of intention, there is an automatic stay of proceedings against creditors. While the stay is in effect, no creditor, including secured creditors and the Crown, has any remedy against the insolvent person or his or her property, or may commence or continue any action, execution or other proceeding, for the recovery of a claim provable in bankruptcy – unless the court lifts the stay (sections 69 and 69.1 of the BIA). The stay continues until it is expired by the terms of the BIA or is terminated by court order. Kevin P. McElcheran, *Commercial Insolvency in Canada,* LexisNexis, Markham, p. 292.

(17) Industry Canada, note 15, p. 30.

(18) Ibid.

(19) Ibid. See also the Standing Senate Committee on Banking, Trade and Commerce, *supra* note 14, p. 100; and the Joint Task Force on Business Insolvency Law Reform, *Report*, 15 March 2002, pp. 27-28.

(20) In this paper, the "commencement of reorganization proceedings" refers to the filing of a notice of intention or a proposal under the BIA or the initial filing of an application under the CCAA.

to the secured creditors likely to be affected by the security or charge, for any period specified in the order. However, in the case of interim financing under the CCAA, the court may only make an order for any period after the first 30 days following the initial application if the monitor reports to the court that the company's cash-flow statement is reasonable. The court may specify that the security or charge ranks in priority over any security or charge of any other secured creditor. The court may also specify that the security or charge ranks in priority over any security or charge arising from a previous order for interim financing, but only with the consent of the person in whose favour the previous order was made.

Bill C-12 makes the following amendments to the above provisions:

- It specifies that an order may only be made on notice to the secured creditors who are likely to be affected by the security or charge.

- It clarifies that the security or charge may apply to "all or part" of the debtor's property.

- It provides that the security or charge may not secure an obligation that exists before the order is made. Therefore, the special status accorded to interim financing loans will only apply to money lent to the company during the period of distress.

- It provides that the court may approve the amount of financing that it considers "appropriate," having regard to the cash-flow statement[(21)] of the debtor. Bill C-12 thus removes the restrictions in the BIA and CCAA as to the duration of financing that may be provided (e.g., with regards to financing after the first 30 days following the commencement of reorganization proceedings).

- The court's authority under Chapter 47 to make an order "on any conditions it considers appropriate" is removed.

(See clause 18, section 50.6(1) BIA; and clause 65, section 11.2(1) CCAA.)

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(21) When filing a proposal with the official receiver, the trustee must include a statement indicating the projected cash-flow of the insolvent person ("cash-flow statement"). The cash-flow statement must be prepared by whoever is making the proposal, and be reviewed for its reasonableness and signed by both the trustee and the person making the proposal. In the same vein, an insolvent person filing a notice of intention with the official receiver must also prepare and file a cash-flow statement, reviewed for its reasonableness by the trustee under the notice of intention, and signed by both the insolvent person and the trustee. Creditors may obtain a copy of the cash-flow statement on request, unless the court orders otherwise (sections 50(6)(a),50(7)-(8), 50.4(2)(a) and 50.4(3)-(4) of the BIA).

Chapter 47 specifies that the cash-flow statement must indicate, on a *weekly* basis, the projected cash-flow of the insolvent person. Bill C-12 changes this to a *monthly* basis (clause 16(1), section 50(6)(a) and clause 17(1), section 50.4(2)(a)).

Bill C-12 also amends the BIA to allow orders for interim financing for individual debtors who are carrying on a business. (Under Chapter 47, individual debtors are excluded from the provisions on interim financing). However, only property acquired for or used in relation to the individual's business may be subject to the security or charge granted by the order for interim financing (clause 18, section 50.6(2)).

In addition, Bill C-12 makes changes to the factors that the court must consider in deciding whether to grant an order for interim financing. Chapter 47 provides that in deciding whether to make an order for interim financing under the BIA, the court must consider the following factors:

a. the period the debtor is expected to be subject to proceedings under the Act;

b. how the debtor's business and financial affairs are to be governed during the proceedings;

c. whether the debtor's management has the confidence of its major creditors;

d. whether the loan agreement will enhance the debtor's prospects as a going concern if the proposal is approved;

e. the nature and value of the debtor's property;

f. whether any creditor will be materially prejudiced as a result of the debtor's continued operations; and

g. where notice of the application is given to the secured creditors, whether the debtor has provided a cash-flow statement for the period ending 120 days after the making of the order.

Under Bill C-12, factor (d) is changed from whether the loan would "enhance the debtor's prospects as a going concern" to whether it would "enhance the prospects of a viable proposal being made in respect of the debtor." This change mirrors the language of the corresponding provision in the CCAA, which provides that the court must consider "whether the loan would enhance the prospects of a viable compromise or arrangement being made in respect of the company" (clause 18, section 50.6(5)(d)).

Under factor (g), the court must consider a report of the trustee as to the reasonableness of the debtor's cash-flow statement (clause 18, section 50.6(5)(g)). Note that the trustee's report must be filed with the official receiver whenever a proposal or notice of intention is filed (see sections 50(6)(b) and 50.4(2)(b) of the BIA).

Bill C-12 makes minor amendments to the language of the corresponding provision in the CCAA. It also directs the court to consider the report of the monitor as to the reasonableness of the company's cash-flow statement, which must be filed under section 23(1)(b)[(22)] of the CCAA (clause 65, CCAA, section 11.2(4)(a)-(g)).

d. Assignment of Agreements (Clauses 28, 65 and 112(10))

Chapter 47 adds provisions to the BIA and the CCAA that allow a debtor to apply to the court for an order assigning rights and obligations under an agreement to another person. Bill C-12 makes a number of important changes to these provisions.

1) BIA

a) Chapter 47

Chapter 47 adds a new section 84.1 to the BIA to allow the court, on the application of a trustee or insolvent person, to make an order assigning the rights and obligations of the insolvent person under any agreement to any other person specified by the court who has agreed to the assignment. In deciding whether to make an assignment, the court must consider the following factors: whether the person to whom the rights and obligations are to be assigned would be able to perform the obligations; and whether it would be appropriate to assign the rights and obligations to that person. The court may not make an assignment if it is satisfied that the insolvent person is in default under the agreement. Moreover, rights and obligations under the following types of agreements cannot be assigned:

- a commercial lease;
- an eligible financial contract (e.g., a derivative);
- a collective agreement;
- rights and obligations that are "not assignable by reason of their nature" (e.g., a personal service contract).

(22) Section 23(1)(b) of the CCAA is enacted by section 131 of Chapter 47. It requires the monitor to review the company's cash-flow statement as to its reasonableness and file a report with the court on his or her findings.

b) Bill C-12

Clause 112(10) of Bill C-12 amends section 84.1 so that only the trustee may make an application for an assignment. In the case of individual bankrupts, applications may only be made if they are carrying on a business, and only rights and obligations in relation to the business may be assigned.

Bill C-12 also provides that the court may not make an order unless it is satisfied that all *monetary defaults in relation to the agreement, other than those arising by reason of the bankruptcy, insolvency or failure to perform a non-monetary obligation, will be remedied on or before the date fixed by the court*. (Under Chapter 47, the court may not make the assignment "unless it is satisfied that the person is in default under the agreement.")

In addition, Bill C-12 amends the list of agreements in respect of which rights and obligations cannot be assigned. In particular, it will be possible under Bill C-12 to assign rights and obligations arising under a commercial lease. However, rights and obligations arising from an agreement entered into on or after the date of bankruptcy will not be assignable. (Rights and obligations arising from an eligible financial contract or a collective agreement will also still not be assignable).

Furthermore, Bill C-12 requires the applicant for an assignment order to send a copy of the order to every party to the agreement.

Note that Chapter 47 provides that where an application is made in respect of a *reorganizing* debtor, the court must consider, before granting the order, whether the debtor would not be able to make a viable proposal without the assignment (section 66(1.1) of the BIA). Bill C-12 replaces this provision with the requirement that the court consider "whether the trustee approves the proposed assignment" (clause 28, section 66(1.1)).

2) CCAA

Chapter 47 adds a new section 11.3 to the CCAA, structured in much the same way as section 84.1 of the BIA, to allow a debtor company to apply for an order for assignment. Clause 65 of Bill C-12 amends section 11.3 of the CCAA to provide that:

- the court may only make an order on notice to the monitor;

- the court must consider, in deciding whether to grant an order, whether the monitor approved the proposed assignment;

- the applicant must send a copy of the order to every party to the agreement; and

- agreements entered into on or after the day on which proceedings commence under the CCAA cannot be assigned.

e. Treatment of Equity Claims
(Clauses 1(7), 19, 20, 49, 54, 69, 71, 99, 105 and 106)

Bill C-12 amends the BIA to exclude the entire class of creditors having "equity claims" from the right to vote on a proposal, unless the court orders otherwise (clauses 19 and 20, sections 54(2)(d) and 54.1).(23) The term "equity claim" has a broad definition under Bill C-12. An "equity claim" is a claim in respect of an equity interest, including a claim for one of the following:

- a dividend or similar payment;

- a return of capital;

- a redemption or retraction obligation;

- a monetary loss resulting from the ownership, purchase or sale of an equity interest, or from the rescission (or in Quebec, the annulment) of a purchase or sale of an equity interest; or

- a contribution or indemnity in respect of any of the above claims (clause 1(7), section 2).

The term "equity interest" is defined as a share in a corporation, or a unit in an income trust – or a warrant, option or another right to acquire a share or unit – other than one that is derived from a convertible debt (clause 1(7), section 2).

Bill C-12 stipulates that the court may not approve of a proposal that provides for the payment of an equity claim, unless the proposal states that all other claims are to be paid in full before the equity claims are paid (clause 99, section 60(1.7) BIA).

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(23) Chapter 47 amends the BIA to exclude, from the class of *unsecured* creditors that may vote on a proposal, those creditors having a claim against the debtor arising from the *rescission of a purchase or sale of a share or unit of a debtor, or a claim for damages arising from the purchase or sale of a unit of the debtor*. Clause 98 of Bill C-12 repeals this provision, replacing it with the much broader exclusion of all creditors having "equity claims" from the right to vote (clauses 19-20).

Note that in the case of bankruptcy, Bill C-12 amends the BIA to subordinate equity claims, as defined above, to all other claims in bankruptcy (clause 49, section 140.1 BIA). Thus, a creditor is not entitled to a dividend in respect of an equity claim unless all other claims have been satisfied.(24)

If the bankrupt is subject to a liability as a result of obtaining property or services by false pretences or fraudulent misrepresentation, a discharge in bankruptcy will not release him from that liability – unless the liability also arises from an equity claim (clause 54, section 178(1)(e) BIA).

Bill C-12 also makes corresponding amendments to the CCAA (clause 69, section 19(2)(d); clause 71, section 22.1; clause 105, section 124(3); and clause 106, sections 6(1) and (8)).

f. Amendment of Debtor's Constating Instrument(25)
(Clauses 21 and 106)

Bill C-12 amends the BIA and CCAA to provide that where the court approves a proposal, compromise or arrangement, it may order that the debtor's constating instrument be amended accordingly, in order to reflect any change that may be made under federal or provincial law (clause 21, section 59(4) BIA; and clause 106, section 6(2) CCAA).

g. Security or Charge Relating to Director's Indemnification
(Clauses 24 and 66)

Chapter 47 introduces new provisions into the BIA and the CCAA to allow a reorganizing debtor to apply to the court for an order declaring that debtor's assets are subject to a security or charge in favour of any director or officer of the debtor. The purpose of these provisions is to indemnify the director or officer against any liability he or she might incur in that capacity after reorganization proceedings are commenced (section 64.1 of the BIA and section 11.51 of the CCAA).

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(24) Under Chapter 47, section 140.1 provides, "a creditor is not entitled to claim a dividend in respect of a claim arising from the *rescission of a purchase or sale of a share or unit of the bankrupt – or in respect of a claim for damages arising from the purchase or sale of a share or unit of the bankrupt* – until all claims of the other claims have been satisfied." Section 140.1 is amended under Bill C-12 to provide, "a creditor is not entitled to a dividend in respect of an *equity claim* until all claims that are not equity claims have been satisfied." Since the definition of "equity claim" in Bill C-12 is broader than a purchase or sale, or a rescission of a purchase or sale, of a share or unit, there is now a broader category of claims that is subordinated under section 140.1.

(25) A constating instrument is a document, issued under federal or provincial legislation, that creates or incorporates a company (e.g., a certificate of incorporation).

Bill C-12 amends these provisions to clarify that the security or charge in favour of the director or officer may apply to "all or part of the property" of the debtor. In addition, it specifies that an order may only be made on notice to the secured creditors likely to be affected by the security or charge.

h. Security or Charge to Cover Certain Costs (Clauses 24 and 66)

Chapter 47 adds a new section 64.2 to the BIA, and a new section 11.52 to the CCAA, to allow the court to make an order declaring that the property of a reorganizing debtor is subject to a security or charge in order to cover the fees and expenses of certain persons, such as legal or financial experts engaged by the trustee or monitor in the performance of his or her duties.

Chapter 47 amends the BIA to provide that the court may specify in the order that the security or charge ranks in priority over the claim of any secured creditor. Bill C-12 adds a corresponding provision to the CCAA (clause 66, section 11.52(2)).

Bill C-12 also provides that the court may only make an order under these provisions on notice to the secured creditors who are likely to be affected by the security or charge. In addition, it clarifies that "all or part" of the property of the debtor may be subject to the security or charge (clause 24, section 64.2(1) BIA; and clause 66, section 11.52(1) CCAA).

Bill C-12 also amends the BIA to allow the court to make an order in respect of an individual debtor who is carrying on a business. Only property acquired for or used in relation to the business may be subject to a security or charge (clause 24, section 64.2(2)).

i. Disclaimer or Resiliation[(26)] of Agreements (Clauses 26 and 76)

Chapter 47 adds provisions to the BIA and the CCAA to permit a reorganizing debtor to disclaim or resiliate certain types of agreements (section 65.11 of the BIA and section 32 of the CCAA). Bill C-12 makes a number of amendments to these provisions.

1) Chapter 47

Under Chapter 47, a debtor may attempt to disclaim or resiliate any agreement to which it is a party as of the date that the reorganization proceedings commence, by giving 30 days' notice to the other parties to the agreement. Within 15 days after being given notice of

(26) To resiliate an agreement is to annul, cancel or repudiate it.

the disclaimer or resiliation, a party to the agreement may apply to the court for a declaration that the disclaimer or resiliation does not apply. The court must make this declaration, unless it is satisfied that a viable proposal could not be made in respect of the debtor without the disclaimer or resiliation of the agreement and of any other agreement that the debtor has already disclaimed or resiliated (BIA, sections 65.11 (1) and (3)-(4); CCAA, sections 32(1) and (3)-(4)).

The provisions on disclaimer and resiliation do not apply to the following contracts: an eligible financial contract; a commercial lease; a collective agreement; a financing agreement, if the debtor is the borrower; or a lease of real property or an immovable if the debtor is the lessor (BIA, sections 65.11(2); CCAA, section 32(2)).

Finally, if an agreement is disclaimed or resiliated, every other party to the agreement is deemed to have a claim for damages as an unsecured creditor (BIA, section 65.11(6); CCAA, section 32(6)).

2) Bill C-12

Bill C-12 makes the following key changes to the provisions on disclaimer and resiliation:

- The debtor is required to provide notice to the trustee (BIA) or monitor (CCAA) that it intends to disclaim, and is not permitted to issue the notice to the other parties unless the trustee or monitor approves of the proposed disclaimer. If the trustee/monitor approves, and the debtor sends notice, the other parties have 15 days to apply to the court for an order that the disclaimer does not apply. However, if the proposal trustee/monitor does not approve of the proposed disclaimer, the reorganizing debtor must apply to the court in order to disclaim the agreement (clause 26, sections 65.11(1) and (3)-(4) BIA; and clause 76, sections 32(1)-(3) CCAA).

- In determining whether to make an order for disclaimer/resiliation (on the application of the debtor), or an order that a disclaimer/resiliation does not apply (on the application of one of the parties to the agreement), the court must have regard to the following factors:
  a. whether the trustee (or monitor) approved the proposed disclaimer or resiliation;
  b. whether the disclaimer or resiliation would enhance the prospects of a viable proposal (or compromise or arrangement) being made in respect of the debtor; and
  c. whether the disclaimer or resiliation would likely cause significant financial hardship to a party to the agreement.

  (Clause 26, section 65.11(5) BIA; and clause 76, section 32(4) CCAA.)

- The debtor is required to provide written reasons for the proposed disclaimer or resiliation to any party to the agreement, within five days of being requested to do so by that party (clause 26, section 65.11(9) BIA; and clause 76, section 32(8) CCAA).

- Section 65.11 of the BIA is extended to apply to individual debtors who carry on a business. (Under Chapter 47, section 65.11 does not apply to individual debtors). However, only business-related agreements may be disclaimed or resiliated (clause 26, section 65.11(2) BIA).

Bill C-12 also clarifies the effective date of the disclaimer or resiliation. If the debtor issues a notice of disclaimer/resiliation, and no party to the agreement makes an application to the court, the agreement is disclaimed or resiliated 30 days after the day on which the debtor gives notice. If an application is made in response to the notice, but the court dismisses the application, the agreement is disclaimed or resiliated within 30 days after the day on which the debtor gives notice. If the debtor applies to the court for an order to disclaim or resiliate the agreement, and the court grants the order, the agreement is disclaimed or resiliated 30 days after the day on which the debtor gives notice or any later day fixed by the court (clause 26, section 65.11(6) BIA; and clause 76, section 32(5) CCAA).

Bill C-12 also clarifies that a party who suffers loss as a result of a disclaimer or resiliation has a "provable claim" (rather than "a claim for damages as an unsecured creditor," as is provided under Chapter 47) (clause 26, section 65.11(8); and clause 76, section 32(7) CCAA).

j. Intellectual Property Agreements (Clauses 26 and 76)

Chapter 47 amends the BIA and the CCAA to provide that if the debtor has, in any agreement, granted the use of intellectual property to a party to the agreement, a disclaimer or resiliation of the agreement does not affect the party's right to use the intellectual property, so long as that party continues to perform its obligations (section 65.11(5) BIA; section 32(5) CCAA).

Bill C-12 enhances the protection afforded to intellectual property licensees when a license of intellectual property is disclaimed. It stipulates that the disclaimer or resiliation does not affect a party's right to use the intellectual property, or to enforce an *exclusive use* of that property during the term of the agreement, *including where a party extends the term of the agreement as of right* – provided that the party continues to perform its obligations under the agreement in relation to the use of the intellectual property (clause 26, section 65.11(7) BIA; and clause 76, section 32(6) CCAA).

k. Restrictions on Sale or Disposal of Assets (Clauses 10, 27 and 78)

Chapter 47 inserts new provisions into the BIA and CCAA that provide guidance for the court in deciding whether to authorize a reorganizing debtor to sell or dispose of its assets outside of the ordinary course of business. Bill C-12 makes significant amendments to these provisions.

1) Chapter 47

Chapter 47 amends the BIA and CCAA to prevent a reorganizing debtor from selling or otherwise disposing of assets outside the ordinary course of business, unless authorized to do so by the court (section 65.13 BIA and section 36 CCAA). In applying to the court for authorization, the debtor must give notice of the application to all secured creditors who are likely to be affected by the proposed sale or disposal of the assets. In deciding whether to grant the authorization, the court must consider the following factors:

a. whether the process leading to the proposed sale or disposition was reasonable in the circumstances;

b. whether the trustee or monitor approved of the process leading to the proposed sale or disposition of the assets;

c. whether the trustee has filed with the court a report stating that in his or her opinion the sale or disposition of the assets is necessary for a viable proposal that will provide a better result for creditors than if the assets were sold or disposed of in a bankruptcy;(27)

d. the extent to which the creditors were consulted in respect of the proposed sale or disposition;

e. the effects of the proposed sale or disposition on creditors and other interested parties; and

f. whether the consideration to be received for the assets is reasonable and fair, taking into account the market value of the assets.

If it grants an authorization, the court may order that the assets be sold or disposed of free and clear of any security, charge or other restriction, but if it so orders, it must also order that the proceeds realized be subject to a security, charge or other restriction in favour of the creditors whose security is affected by the order.

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(27) In the case of the CCAA, this factor is worded as "whether the monitor has filed with the court a report stating that in his or her opinion the sale or disposal of the assets would be more beneficial to the creditors than if the sale or disposal took place under the *Bankruptcy and Insolvency Act*."

Chapter 47 places additional limitations on the sale or disposal of assets to a person who is related to the debtor. The court, in addition to taking into account factors (a)-(f) listed above, may only grant authorization if it is satisfied that good faith efforts were made to sell or dispose of the assets to an unrelated person, and the consideration to be received is superior to the consideration that would be received under all other offers actually received in respect of the assets. Under Chapter 47, a person who is "related" to the debtor includes a person who controls the debtor, as well as directors and officers and persons who are related to directors and officers.

2) Bill C-12

Clauses 27 and 78 of Bill C-12, amending the BIA and the CCAA, respectively, make a number of key amendments. In particular, Bill C-12:

- Stipulates that notwithstanding any requirement for shareholder approval – including any requirement under provincial or federal law – the court may authorize a sale or disposition of assets even if shareholder approval is not obtained (section 65.13(1) BIA; and section 36(1) CCAA).

- Provides that where the court orders that the assets be sold or disposed of free and clear of any security, charge or other restriction, it must also order that the proceeds of the sale or disposal, *or other assets of the debtor*, are subject to a security, charge or restriction in favour of the affected creditors (section 65.13(7) BIA; and section 36(6) CCAA).

- Clarifies that in order to obtain authorization of a sale or disposal to a related party, the related party must offer consideration that is superior to any other offer *made in accordance with the process leading up to the proposed sale*. It also provides that persons who are related to the debtor include those who are related to any person who has, or has had, control of the debtor (sections 65.13(5)(b) and (6) BIA; and sections 36(4)(b) and (5) CCAA).

- Provides that in the case of a debtor that is an employer, the court may only grant an authorization to sell or dispose of assets if it is satisfied that the debtor can and will make any payments in respect of unpaid wage claims and unremitted pension plan contributions that would have been required in order to obtain court approval of the reorganization (section 65.13(8) BIA; and section 36(7)[(28)] CCAA).

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(28) It should be noted that there is a small drafting error under the proposed section 36(7) of the CCAA. That section reads: "The court may grant the authorization only if the court is satisfied that the company can and will make the payments that would have been required under paragraphs 6(4)(a) and (5)(a) if the court had sanctioned the compromise or arrangement" (emphasis added). Sections 6(4)(a) and 6(5)(a) of the CCAA, as enacted by Chapter 47, are the provisions that require the reorganizing debtor to meet its obligations with respect to unpaid wage claims and unremitted pension plan contributions. However, these provisions are renumbered under clause 106 of Bill C-12 as paragraphs 6(5)(a) and 6(6)(a). There is no 6(4)(a).

Bill C-12 also amends the BIA to ensure that section 65.13 applies to individual debtors who are carrying on a business. (Under Chapter 47, section 65.13 does not apply to individual debtors.) However, the court may only authorize the sale or disposition of assets acquired for or used in relation to the business (section 65.13(2)).

Note that Bill C-12 also amends the BIA to reword the third factor (factor (c)) that the court must consider in deciding whether to make an authorization. The court must consider "whether the trustee filed in court a report stating that in their opinion the sale or disposition would be *more beneficial to the creditors than a sale or disposition under a bankruptcy*" [emphasis added], reflecting the language of the CCAA (section 65.13(4)(c)).

It should also be mentioned that Chapter 47 adds new provisions to the BIA (sections 30(5)-(6)) to require a trustee in bankruptcy to obtain court authorization in order to sell or dispose of property to persons who are related to the bankrupt. In the case of a bankrupt other than an individual, a "person who is related to the bankrupt" includes a person who controls the bankrupt; directors and officers; and persons who are related to directors and officers. In deciding whether to grant the authorization, the court is required to consider, among other things, "whether the consideration to be received is superior to the consideration that would actually be received under all other offers actually received in respect of the property" (section 30(6)(f)).

Clause 10 of Bill C-12 clarifies that a "person related to the bankrupt" includes a person who "has, or has had, directly or indirectly, control in fact" of the bankrupt, and any person related to such a person. Furthermore, it replaces section 30(6)(f) with a requirement for the court to consider "whether the consideration to be received is superior to the consideration that would be received under *any other offer made in accordance with the process* leading to the proposed sale or disposition of the property."

l. Avoidance Transactions: Preferences and Transfers at Undervalue (Clauses 1(4), 2, 16(3), 41-43, 72(2) and 78)

1) Preferences

Sections 95 and 96 of the BIA are aimed at preventing a bankrupt from according a "fraudulent preference" to a creditor. A "fraudulent preference" is a transaction with a creditor of the debtor that occurs less than three months prior to the initial bankruptcy event, when the debtor is insolvent, with a view to giving that creditor a preference over other creditors of the

debtor (section 95(1)). These transactions may be challenged by the trustee in bankruptcy. The court may reverse a transaction attacked by the trustee if it finds that the transaction was undertaken with a view to giving the creditor a preference over other creditors. Where the transaction has the effect of preferring the creditor, a rebuttable presumption arises that the transaction was undertaken with a view to giving a preference to a creditor. Under section 96, if the transaction is in favour of a creditor that is "related" to the debtor, the reference period for attacking the transaction is one year instead of three months (section 96).

Chapter 47 amends section 96 of the BIA to provide that the reference period for attacking the transaction is one year where the transaction has the effect of giving a creditor who is "not at arm's length" with the debtor a preference over other creditors.

Related persons, as defined in the BIA, are deemed not to deal with each other at arm's length. However, it is a question of fact whether persons who are not related to each other are dealing at arm's length (sections 3-4 of the BIA). Therefore, the amendment made by Chapter 47 has the effect of expanding the group of creditors who are covered by the one-year reference period (i.e., it includes unrelated persons who are not dealing at arm's length). On the other hand, it is unclear from the wording of the proposed section 96 as to whether the trustee is required to establish a preferential intent in order to extend the reference period from three months to one year.(29)

Bill C-12 restructures this provision of the BIA in order to clarify its effect (clause 42, section 95(1)). It provides that in the case of arm's length creditors, the reference period is three months. The trustee must establish that the transaction was undertaken with a view to giving the creditor a preference. However, if the transaction has the effect of preferring the creditor, a rebuttable presumption arises that the transaction was undertaken with a view to preferring the creditor.

In the case of non-arm's length creditors, the reference period is one year. The trustee only has to establish that the transaction had the effect of giving the creditor a preference. The intention underlying the transaction is irrelevant.(30)

The general presumption under the BIA is that related persons are deemed not to deal with each other at arm's length. Bill C-12 specifies that, for the purposes of the preferences section of the Act, related persons are deemed not to deal with each other at arm's length

(29) Shea, note 10.

(30) Ibid.

in the absence of evidence to the contrary (clause 2, section 4(5) BIA). This means that, in some cases, related persons will be able to demonstrate that they are dealing with each other at arm's length. Note that "related persons" include corporations under common or related control.

Bill C-12 includes "a provision of services" in the group of transactions that may be attacked by the trustee (clause 42, section 95(1)). This type of transaction is not currently covered by the BIA.

2) Transfers at Undervalue

Chapter 47 repeals the provisions of the BIA on settlements and reviewable transactions and replaces them with new provisions on "transfers at undervalue"[(31)] (see clauses 71-73 and 76 of Chapter 47).

Under Chapter 47, the court may, on the application of the trustee, inquire into whether a transaction entered into by the debtor was a transfer at undervalue and whether or not the other party was at arm's length with the debtor (clause 73, section 96.1 BIA). The term "transfer at undervalue" is defined as a transaction in which the consideration received by a person is conspicuously less than the fair market value of the property or services sold or disposed of by the person in the transaction (Chapter 47, clause 2(5), section 2 BIA). Where the court finds that the transaction was a transfer at undervalue, it may, subject to certain conditions, give judgment to the trustee against the other party to the transaction and/or against any other person that is privy to the transaction with the debtor, for the difference between the actual consideration given or received and the fair market value, as determined by the court, for the property or services concerned in the transaction. However, the conditions that must be met in order to grant such an order differ depending on whether the court finds that the parties were or were not at arm's length.

If the court finds that the parties were at arm's length, the court may only grant the order if:

1. the transaction occurred during the period beginning one year before the date of the initial bankruptcy event and ending on the date of bankruptcy;

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(31) Ibid.

Section 91 of the BIA deals with settlements, and section 100 of the BIA deals with reviewable transactions. These provisions are repealed by clauses 71 and 76, respectively, of Chapter 47. For a discussion of sections 91 and 100 of the BIA, please see McElcheran, note 16, pp. 63-64 and 69-70.

2. the debtor was insolvent at the time of, or was rendered insolvent by, the transaction; *and*

3. the debtor intended to defeat the interests of creditors.

If the court finds that the parties were not at arm's length, criteria (2) and (3) do not apply. The court may thus grant the order if the transaction occurred during the period beginning one year before the date of the initial bankruptcy event and ending on the date of bankruptcy.

If the parties were not at arm's length, the court may also grant the order if:

1. the transaction occurred in the period beginning *five years* before the date of the initial bankruptcy event and ending one year before the date of the initial bankruptcy event; *and*

2. the debtor was insolvent at the time of the transaction, or rendered insolvent by the transaction; *or* the debtor intended to defeat the interests of the creditors.

Clause 43 of Bill C-12 makes the following amendments to the provisions on transfers at undervalue:

- The amount of payment that the court may order is the difference between the "value of the consideration received by the debtor and the value of the consideration given by the debtor." (Under Chapter 47, the amount of payment is the difference between the actual consideration given or received and the fair market value, as determined by the court, for the property or services concerned.) Payment must be made to the estate, rather than to the trustee.

- The court is also empowered to declare that a transfer at undervalue is void as against the trustee (or, in Quebec, may not be set up against the trustee).

- The conditions that apply for making an order remain the same; however, when establishing the intent of the debtor, the trustee may show that the debtor intended to "*defraud*, defeat or *delay*" a creditor.

- A "person who is privy" is defined as a person who is not dealing at arm's length with a party to the transfer and, by reason of the transfer, directly or indirectly receives a benefit or causes a benefit to be received by another person.

Clause 1(3) of Bill C-12 amends the definition of "transfer at undervalue" to be a *disposition of property* or a *provision of services* for which the consideration received by the debtor is conspicuously less than the fair market value of the consideration given by the debtor. It also includes a disposition of property or a provision of services for which *no* consideration is received by the debtor.

Clause 2 of Bill C-12 also amends section 4(5) of the BIA to provide that for the purposes of establishing whether persons are dealing at arm's length in a transfer at undervalue, persons who are related to each other are, in the absence of evidence to the contrary, deemed not to deal with each other at arm's length. Thus, the general presumption that related persons are not dealing with each other at arm's length may be rebutted. The amended definition of "arm's length" parties will help to ensure that legitimate family law agreements (e.g., for spousal or child support) are not inadvertently captured by the avoidance transaction provisions of the BIA.(32)

3) Avoidance Transactions in Reorganizations

The BIA provisions on avoidance transactions apply not only in bankruptcies, but also in commercial proposals (i.e., reorganizations), except where the proposal provides otherwise (section 101.1 of the BIA). Bill C-12 amends the CCAA to ensure that the avoidance transaction provisions of the BIA also apply to reorganizations under the CCAA, unless the compromise or arrangement in question provides otherwise (clause 78, section 36.1 CCAA).

Bill C-12 also provides that section 38 of the BIA applies to compromises and arrangements under the CCAA, unless the compromise or arrangement provides otherwise (clause 78, section 36.1 CCAA). Section 38 of the BIA allows a creditor to apply to the court for an authorization to institute a proceeding at his or her own expense, if the creditor believes that the proceeding would be for the benefit of the estate and the trustee refuses or neglects to act.(33)

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(32) Speaking Notes of Mr. Colin Carrie, M.P., note 5.

(33) Section 38 provides as follows:

38.(1) Where a creditor requests the trustee to take any proceeding that in his opinion would be for the benefit of the estate of a bankrupt and the trustee refuses or neglects to take the proceeding, the creditor may obtain from the court an order authorizing him to take the proceeding in his own name and at his own expense and risk, on notice being given the other creditors of the contemplated proceeding, and on such other terms and conditions as the court may direct.

(2) On an order under subsection (1) being made, the trustee shall assign and transfer to the creditor all his right, title and interest in the chose in action or subject-matter of the proceeding, including any document in support thereof.

(3) Any benefit derived from a proceeding taken pursuant to subsection (1), to the extent of his claim and the costs, belongs exclusively to the creditor instituting the proceeding, and the surplus, if any, belongs to the estate.

(4) Where, before an order is made under subsection (1), the trustee, with the permission of the inspectors, signifies to the court his readiness to institute the proceeding for the benefit of the creditors, the order shall fix the time within which he shall do so, and in that case the benefit derived from the proceeding, if instituted within the time so fixed, belongs to the estate.

Finally, if a proposal, compromise or arrangement provides that the avoidance transactions provisions of the BIA do not apply, the trustee or monitor must now include, in his or her report to the court regarding the financial and business affairs of the company, an opinion as to the reasonableness of this decision. The monitor has the same duty where the compromise or arrangement provides that section 38 of the BIA does not apply (clause 16(3), section 50(10)(b) BIA; and clause 72(2), section 23(2)(d.1) CCAA).

m. Liability of Insolvency Professionals (Clauses 9(2)-(3) and 67)

Section 14.06(1.2) of the BIA shields a trustee[34] from personal liability when carrying on the business of the debtor, or continuing to employ the debtor's employees, in respect of any claims that arose on or before his or her appointment. The protection applies despite anything in provincial or federal law.

Chapter 47 amends this provision to clarify that the trustee is not liable for any "debt or liability, *present or future*" to which the debtor is subject on the date that the trustee is appointed.

Bill C-12 replaces the amendment made by Chapter 47. It shields trustees carrying on the business of the debtor from liabilities regarding the current or former employees of the debtor – including liabilities relating to a pension plan – if the liabilities exist before the trustee is appointed or are calculated by reference to a period before the appointment. However, this provision does not affect the liability of a successor employer other than a trustee (clauses 9(2)-(3)).

Bill C-12 makes a virtually identical amendment to the CCAA to protect monitors from personal liability when carrying on the business of the debtor company (clause 67, sections 11.8(1)-(2.1) CCAA).

n. Cross-border Insolvencies (Clauses 59-60 and 80-81)

Chapter 47 amends the BIA and CCAA to adopt procedures for dealing with cross-border insolvency proceedings based on the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-border Insolvency (Part XIII of the BIA and Part IV of the CCAA).

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(34) The term "trustee" is defined in this context to include a trustee in bankruptcy or in a proposal, an interim receiver or a receiver. Under Chapter 47, it also includes "any other person who has been lawfully appointed to take, or has lawfully taken, possession or control of any property of an insolvent person or a bankrupt that was acquired for, or used in relation to, a business carried on by the insolvent person or bankrupt" (clause 17). Bill C-12 does not affect this amendment.

Under the new provisions, when a Canadian court issues an order recognizing a foreign proceeding, the court must cooperate, to the maximum extent possible, with the foreign representative and the foreign court involved. If proceedings under the BIA or the CCAA have also been commenced in respect of the debtor, every person who has any duties, powers or functions in those proceedings must cooperate, to the maximum extent possible, with the foreign court and the foreign representative.

Bill C-12 adds new provisions to the BIA and the CCAA to specify that cooperation may be provided by any appropriate means, including the following: the appointment of a person to act at the direction of the court; the communication of information by any means considered appropriate by the court; the coordination of the administration and supervision of the debtor's assets and affairs; the approval or implementation by courts of agreements concerning the coordination of proceedings; and the coordination of concurrent proceedings regarding the same debtor (clause 59, section 275(3) BIA; and clause 80, section 52(3) CCAA).

Under Chapter 47, section 284(2) of the BIA and section 61(2) of the CCAA stipulate that the parts of those acts on cross-border insolvency do not require the court to "make any order that is not in compliance with the laws of Canada or to enforce any order made by a foreign court." Bill C-12 broadens this exception to provide that the new parts do not "prevent the court from refusing to do something that would be contrary to public policy" (see clauses 60 and 81).

3. Other Amendments to the BIA

a. Date of the Initial Bankruptcy Event (Clause 1(6))

Bill C-12 expands the definition of "date of the initial bankruptcy event" in section 2 of the BIA to include proceedings under the CCAA. Thus, the "date of the initial bankruptcy event" will include the commencement of reorganization proceedings under either the BIA or the CCAA. This is important for the calculation of time periods in various proceedings under the BIA.

b. Application of Legislation Providing for Compromises or Arrangements (Clause 28(2))

Bill C-12 stipulates that the provisions of the BIA concerning proposals may be applied together with the provisions of any federal or provincial Act that authorizes or provides for the sanction of compromises or arrangements between a corporation and its shareholders (clause 28(2), section 66(1.4) BIA).

c. Application to Revoke or Vary a Decision (Clause 46)

The BIA provides the chair of a meeting of creditors with the power to admit or reject a proof of claim for the purpose of voting at a meeting of creditors. A decision of the chair may be appealed to the court.

Bill C-12 adds a new section 115.1 to the BIA to allow the court, on an application to revoke or vary a decision that could affect the outcome of a vote of creditors, to make any order that it considers appropriate, including an order that:

- suspends the outcome of the vote pending the court's decision on the application; or
- redetermines the outcome of the vote.

4. Other Amendments to the CCAA

a. Critical Supplier (Clause 65)

Chapter 47 adds provisions to the CCAA, but not to the BIA, to allow the debtor to apply to the court for an order declaring a person to be a "critical supplier" of goods and services to the debtor (section 11.4). The court may make an order requiring the critical supplier to supply any goods or services specified in the order, on any terms and conditions that are consistent with the supply relationship or that the court considers reasonable. If the court makes such an order, it must declare that the debtor's property is subject to a security or charge in favour of the critical supplier, in an amount equal to the goods or services supplied under the terms of the order. The court may specify that the security or charge ranks in priority over the claim of any other secured creditors of the company.

Bill C-12 amends the CCAA to provide that an application for a critical supplier order may only be made on notice to the secured creditors who are likely to be affected by the security or charge. It also clarifies that a security or charge may apply to "all or part" of the debtor's company (clause 65, sections 11.4(1) and (3)). Note that Bill C-12 does not insert corresponding provisions for a "critical supplier order" into the BIA.

b. Voting on Compromise or Arrangement – Related Creditor (Clause 71)

Clause 71 of Bill C-12 amends the CCAA to provide that a creditor who is related to the debtor company may vote against, but not for, a compromise or arrangement relating to the company (section 22(3) CCAA).

c. Restrictions on Terminating Contracts With the Debtor Company (Clause 77)

The BIA generally prohibits a person from terminating or amending an agreement with a reorganizing debtor, or claiming an accelerated payment or forfeiture of the term under the agreement, for the sole reason that the debtor is undergoing reorganization (i.e., a notice of intention or proposal has been filed in respect of the debtor), or that it is insolvent (section 65.1).

Chapter 47 introduces similar provisions into the CCAA (section 34). Under Chapter 47, the prohibition against terminating or amending an agreement with a debtor company applies where the sole motivation for doing so is that "an order has been made under the Act in respect of the company." Bill C-12 amends this so that the prohibition applies where the sole motivation for the termination or amendment of the agreement is either that proceedings have been commenced under the Act, or because the company is insolvent (clause 77, sections 34(1)-(3)).

Second, Bill C-12 clarifies that the prohibition does not apply to an eligible financial contract, or prevent a member of the Canadian Payments Association from ceasing to act as a clearing agent or group clearer for the insolvent company (clause 77, sections 34(7)(a)-(b)). (These two exceptions also apply under the parallel provision of the BIA.[35])

Third, Bill C-12 provides that the prohibition against termination/amendment does not apply to prevent a lessor of aircraft objects under an agreement with the company from taking possession of the aircraft objects, provided that certain conditions are met (clause 77,

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(35) See section 65.1(7)(a)-(b) of the BIA.

section 34(4)(c)).[36] These provisions are based on the International Institute for the Unification of Private Law (UNIDROIT) Convention on International Interests in Mobile Equipment and the Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment. In particular, the lessor may take possession of the aircraft objects after the expiry of 60 days from the date that proceedings commence under the CCAA – unless the debtor company has done all of the following things during that 60-day period:

1. Remedied the default of every other obligation under the agreement (other than a default constituted by the commencement of proceedings under the Act or the breach of a provision in the agreement related to the company's financial condition).

2. Agreed to perform the obligations under the agreement until the proceedings under the CCAA end (other than the obligation not to become insolvent or an obligation related to the company's financial condition).

3. Agreed to perform all of the obligations arising under the agreement after the proceedings under the CCAA end.

Furthermore, if the debtor company defaults in performing an obligation under the agreement at any time after the expiry of the first 60-day period – other than an obligation not to become insolvent or an obligation relating to the company's financial condition – the lessor may seize the aircraft objects.

Finally, if the debtor company defaults, at any time after proceedings commence, in protecting or maintaining the aircraft objects in accordance with the agreement, the lessor may seize the objects.

B. Consumer Insolvency Issues

1. Revival of Consumer Proposals Deemed Annulled (Clause 30)

Under the BIA, a consumer debtor[37] may file a proposal to his or her creditors as an alternative to filing for bankruptcy.

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(36) Note that clause 43(2) of Chapter 47 adds similar provisions to the BIA.

(37) A "consumer debtor" is currently defined as a bankrupt or insolvent individual whose aggregate debts, excluding any debts secured by the individual's personal residence, do not exceed $75,000 (section 66.11). Chapter 47 raises this limit to $250,000 (clause 46).

Chapter 47 provides for the revival of a consumer proposal, made by a person other than a bankrupt, which has been deemed to be annulled(38) under the Act due to the debtor's default in payment. Bill C-12 makes some slight changes to these provisions.

Under Chapter 47, there are two ways that a consumer proposal deemed annulled can be revived – automatically, or by count order.

First, an administrator may, if he or she considers it appropriate to do so in the circumstances, send a notice to creditors within 10 days after the day on which the proposal is deemed to be annulled, informing them that the consumer proposal will be automatically revived within 45 days of the date it was deemed to be annulled, unless one of the creditors files a notice of objection in the prescribed form to the revival. If no notice of objection is filed during the 45-day period, the consumer proposal is automatically revived. However, if a creditor files an objection, the administrator must send to the official receiver and each of the creditors a notice informing them that the proposal is not going to be automatically revived on the expiry of the 45-day period.

Second, the administrator may, at any time, apply to the court, with notice to the creditors and official receiver, for an order reviving the consumer proposal. The court may, if it considers it appropriate to do so in the circumstances, make an order reviving the proposal, on any terms that it considers appropriate.

Bill C-12 changes the time periods that apply for automatic revival of a proposal. Specifically, in order for the consumer proposal to be automatically revived, the administrator must send notice to the creditors within 30 days, or any other number of days prescribed by regulation. The period during which a notice of objection may be filed is raised from 45 to 60 days (clause 30, section 66.31(6)).

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(38) Under section 66.31 of the BIA, unless the court has previously ordered otherwise, a consumer proposal is deemed to be annulled as follows: payments under the proposal are to be made monthly or more frequently, and the debtor is in default to the extent of three months' payments; or payments are to be made less frequently than monthly and the consumer debtor is in default for more than three months on any payment. Unless the court orders otherwise, if a proposal is deemed annulled, the consumer debtor may not make another consumer proposal and is not entitled to a stay of proceedings against the creditors. The rights of the creditors are correspondingly revived for the amount of their claims, less any dividends received (section 66.32).

Chapter 47 makes slight changes to the circumstances under which a proposal is deemed to be annulled. Specifically, unless the court otherwise orders, a consumer proposal is deemed to be annulled on the day that the debtor is in default for an amount that is at least equal to *three payments*, if payments under the proposal are to be made monthly or more frequently; or three months after the day on which the consumer debtor is in default in respect of any payment, if payments are to be made less frequently than monthly.

2. Exemption of RRSPs and RRIFs (Clause 32(1))

The BIA governs the distribution of assets when a person becomes bankrupt. The general rule is that all assets belonging to a bankrupt person become the property of the bankruptcy trustee and available to satisfy creditors' claims. However, certain classes of property ("exempt property") continue to belong to the debtor. Under section 67(1)(b) of the BIA, property that is exempt from execution or seizure under any laws applicable in the province or territory within which the property is situated and within which the bankrupt resides, is also exempt from seizure in bankruptcy.

Due to this provision, funds invested in Registered Pension Plans (RPPs) are exempt from seizure in bankruptcy by virtue of provincial and federal pension benefits legislation.(39) Registered Retirement Savings Plans (RRSPs) in the form of a contract with an insurance company and where a spouse, child, parent, grandparent, or grandchild of the plan owner is named as a beneficiary are exempt from seizure on bankruptcy under laws governing insurance.(40) Locked-in RRSPs holding money that was transferred from a pension plan on termination of employment after pension rights have vested are exempt from seizure on bankruptcy under pension legislation.(41) By contrast, RRSPs held by banks, brokerages, or mutual funds, or in self-directed RRSP accounts, are not exempt from seizure in the event of bankruptcy.(42) These RRSPs vest in the trustee in bankruptcy on the bankruptcy of the plan owner. The money held in the RRSP becomes available for distribution to creditors.

In order to ensure the consistent treatment of retirement savings vehicles, Chapter 47 exempts property in RRSPs and Registered Retirement Income Funds (RRIFs), as those terms are defined in the *Income Tax Act*, from seizure in bankruptcy. However, to prevent abuse of the exemption, property contributed to the RRSP or RRIF in the 12 months before the date of bankruptcy, or such longer period prescribed by the court, is subject to seizure. Finally, the exemption of RRSPs and RRIFs is subject to "any prescribed conditions and limitations" (section 67(1)(b.3) of the BIA).

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(39) Industry Canada, note 15, p. 57.

(40) Margaret Smith, *Registered Retirement Savings Plans (RRSPs) and Bankruptcy*, PRB 01-32E, Parliamentary Information and Research Service, Library of Parliament, Ottawa, 21 March 2002, p. 6.

(41) Ibid.

(42) Ibid.

Bill C-12 makes the amendments to section 67(1)(b.3) that were requested by the Bloc Québécois in the 1st Session of the 39th Parliament, in order to respect the provisions of the Quebec *Civil Code* and *Code of Civil Procedure* regarding the seizure of RRSPs and RRIFs.(43) Under Bill C-12:

- Section 67(1)(b.3) specifies that the exemption of RRSPs and RRIFs does not restrict the generality of paragraph 67(1)(b). As mentioned above, paragraph 67(1)(b) of the BIA exempts from seizure in bankruptcy any property that is also exempt from seizure under any laws applicable within the province or territory where the property is situated and within which the debtor resides. Thus, if provincial/territorial law protects contributions within the 12 months preceding the date of bankruptcy, the clawback will not apply.

- The power of the court to extend the 12-month clawback period is removed.

- The Government no longer has the authority to prescribe conditions or limitations on the exemption. Therefore, the Government may not, for example, require that an RRSP be "locked in" until retirement in order to be protected.

- The Government is authorized to apply the exemption in section 67(1)(b.3) to any other plan prescribed by regulation.

3. Family Law Claims (Clause 32(2))

Section 67(1)(c) of the BIA stipulates that "all property, wherever situated, of the bankrupt at the date of his bankruptcy or that may be acquired by or devolve on him before his discharge" vests in the trustee for distribution to the bankrupt's creditors, subject to the specific exemptions listed in the BIA. Chapter 47 amends this provision to specify that the property subject to seizure includes any refund owing to the bankrupt under the *Income Tax Act* in the year in which the person became a bankrupt, except for any portion of the refund that is not subject to the operation of the BIA.

Bill C-12 clarifies that any portion of an income tax refund that is garnishable money, to be paid under a garnishee summons for which the bankrupt is the judgment debtor and that has been served under the *Family Orders and Agreements Enforcement Assistance Act*, is not subject to seizure. Thus, any part of the bankrupt's income tax refund that is being garnished in order to satisfy his legal obligations under the *Family Orders and Agreements Enforcement Assistance Act* (e.g., child and spousal support) cannot be touched by the trustee in bankruptcy (clause 32(2), section 67(1)(c)(ii) BIA).

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(43) This issue is discussed in the introduction to this paper.

4. Contributions of Surplus Income to the Bankrupt's Estate (Clauses 33(1) and 33(5))

Under section 68 of the BIA, trustees are required to collect a prescribed portion of the bankrupt's surplus income for the benefit of the debtor's estate and, by extension, for the benefit of creditors. Trustees calculate the amount of surplus income a debtor may have with reference to standards published by the Superintendent of Bankruptcy, taking into account the personal and family situation of the bankrupt. The Superintendent's standards are based on the Low Income Cut-off measures produced annually by Statistics Canada.(44)

A requirement to pay surplus income is currently enforceable against all property of the bankrupt – other than property that is exempt from seizure under provincial or territorial law, and goods and services tax credit payments and other prescribed payments relating to the essential needs of the individual (section 68(2)(b) BIA).

Chapter 47 empowers the trustee to enforce surplus income payment requirements against all of the bankrupt's property, including property that is exempt from seizure under provincial or territorial law and goods and services tax credit payments. Bill C-12 amends this power to provide that the trustee may enforce surplus income payments only against the bankrupt's "total income" (clause 33(5), section 68(15) BIA). A bankrupt's "total income," as defined by Chapter 47 and amended by Bill C-12, is earned only between the date of the bankruptcy and the date of discharge (Bill C-12, clause 33(1), section 68(2)). It includes revenues of whatever nature or from whatever source that are earned during that period, including those received as damages for wrongful dismissal, as a pay equity settlement, or as a payment related to workers' compensation. However, an amount received by the bankrupt between the date of bankruptcy and the date of discharge, as a gift, legacy, inheritance or any other windfall, is excluded from the definition of "total income."

The definition of "total income" specifically applies despite sections 67(1)(b) and 67(1)(b.3) of the BIA (as enacted by Bill C-12). These sections exempt, from the property of the bankrupt that is distributable to creditors, assets that are exempt from seizure under provincial or territorial law, as well as RRSP/RRIF contributions. The fact that the definition of "total income" applies despite these two exemptions indicates that these assets are subject to enforcement for surplus income payments. However, the definition of "total income" is not

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(44) Office of the Superintendent of Bankruptcy, Personal Insolvency Task Force, *Final Report*, August 2002, p. 45.

worded to apply despite any of the remaining exemptions listed in section 67(1), such as goods and services tax payments or payments relating to the essential needs of the individual. This definition suggests that the trustee cannot enforce surplus income payments against property falling under the remaining exemptions of section 67(1).

5. Income Tax Debt (Clause 53(2))

Chapter 47 amends the BIA to impose new restrictions on the discharge of bankrupts who have at least $200,000 in personal income tax debt, where the debt represents more than 75% of the total unsecured proven claims.

Bill C-12 clarifies that "personal income tax debt" does not include an amount for which an individual is personally liable to pay in his or her capacity as a current or former director of a corporation, as a result of an obligation of the corporation (clause 53(2), section 172.1(8)).

6. Discharge of Student Loans(45) (Clause 107(2))

Prior to 1997, student loan debt was treated in the same way as other consumer debt. Student loans were discharged along with other debts, provided the trustee or creditor did not believe the debtor was abusing the system, in which case he or she could oppose the discharge.

Amendments to the BIA that took effect in 1997 changed the status of student loan debts by making them non-dischargeable if a student filed for bankruptcy before ceasing full- or part-time studies or within two years after studies ended. A student who went bankrupt during the two-year period, however, could apply to the court at the end of the two-year period to discharge the student loan. The court could order a discharge if the student was able to demonstrate that he or she had acted in good faith and could not repay the loan due to financial difficulty. Those who filed for bankruptcy after the two-year period could have their student loans discharged as part of the normal bankruptcy process.

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(45) This summary of 1997 and 1998 amendments to the BIA is adapted from Margaret Smith, *Treatment of Student Loans under Canadian Bankruptcy Law*, PRB 01-26E, Parliamentary Information and Research Service, Library of Parliament, Ottawa, 18 March 2002.

In 1998, the student loan non-dischargeable period was extended from 2 years to 10 years. Therefore, student loan debt is not discharged by a bankruptcy if the bankruptcy occurs within 10 years after a person ceases being a student. However, the bankrupt may apply to the court after the expiry of the 10-year period for an order discharging the student loan debt (sections 178(1)(g) and 178(1.1) of the BIA).(46) Furthermore, those who file for bankruptcy after the 10-year period can have their student loans discharged as part of the normal bankruptcy process.

Chapter 47 reduces the discharge prohibition period from 10 years to 7 years. Furthermore, the court may, on the application of the bankrupt, discharge the debt five years after the completion of studies, if the court is satisfied that the bankrupt has acted in good faith and will continue to experience such financial difficulty that he or she will be unable to repay the debt.

Bill C-12 clarifies that when the new seven-year discharge period comes into force, it will not only apply to individuals who file for bankruptcy after that date, but also to those who have already filed for bankruptcy and have not been discharged. (The five-year waiting period will apply to all bankrupts, past, present and future.(47))

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(46) Sections 178(1)(g) and 178(1.1) of the BIA are worded as follows:

> 178(1) An order of discharge does not release the bankrupt from
>
> …(*g*) any debt or obligation in respect of a loan made under the *Canada Student Loans Act*, the *Canada Student Financial Assistance Act* or any enactment of a province that provides for loans or guarantees of loans to students where the date of bankruptcy of the bankrupt occurred
>
> (i) before the date on which the bankrupt ceased to be a full- or part-time student, as the case may be, under the applicable Act or enactment, or
>
> (ii) within ten years after the date on which the bankrupt ceased to be a full- or part-time student; or
>
> (*h*) any debt for interest owed in relation to an amount referred to in [paragraph (*g*)].
>
> (1.1) At any time after ten years after a bankrupt who has a debt referred to in paragraph (1)(*g*) ceases to be a full- or part-time student, as the case may be, under the applicable Act or enactment, the court may, on application, order that subsection (1) does not apply to the debt if the court is satisfied that
>
> (*a*) the bankrupt has acted in good faith in connection with the bankrupt's liabilities under the loan; and
>
> (*b*) the bankrupt has and will continue to experience financial difficulty to such an extent that the bankrupt will be unable to pay the liabilities under the loan.

(47) *Speaking Notes for the Minister of Labour's Appearance before the Senate Standing Committee on Banking, Trade and Commerce on Bill C-12: An Act to Amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and Chapter 47 of the Statues of Canada, 2005*, 29 November 2007.

7. Ipso Facto Clauses (Clause 112(10))

According to the Personal Insolvency Task Force,[48] it is common for consumer agreements with some creditors – particularly banks and utility companies – to contain a provision that entitles the creditor to terminate the agreement immediately if the consumer goes bankrupt, even if the consumer is not in default under the agreement at the time of bankruptcy.[49] These types of clauses are referred to as "ipso facto clauses."[50] Thus, banking services may be terminated, or utility services disconnected, as soon as consumers go bankrupt. Section 66.34 of the BIA nullifies such clauses in the event an insolvent person files a consumer proposal. However, this provision does not apply in the event of bankruptcy.

Chapter 47 amends the BIA to prohibit a person from terminating or amending, or claiming an accelerated payment or forfeiture of the term, under any agreement with a bankrupt individual, for the sole reason of the individual's bankruptcy or insolvency (section 84.2 BIA).

However, Bill C-12 amends this provision to stipulate that the prohibition does not apply to an eligible financial contract (e.g., a derivative). Furthermore, the prohibition does not prevent a member of the Canadian Payments Association from ceasing to act as a clearing agent or group clearer for an insolvent person (section 84.2(7) BIA).

8. Directions to Pay as a Condition of Discharge (Clause 101)

Chapter 47 amends the BIA to provide that where the court requires a bankrupt to pay money as a condition of discharge from bankruptcy, it may also direct the bankrupt to pay the money to any creditor, class of creditors, and/or to the trustee, in any amount and manner that the court considers appropriate. Clause 101 of Bill C-12 repeals this provision.

9. Section 175 of the BIA (Clause 102)

Section 175 of the BIA provides that a statutory disqualification on account of bankruptcy ceases if the bankrupt obtains a discharge from the court with a certificate to the effect that the bankruptcy was caused by misfortune without any misconduct on the part of the bankrupt. The court may grant such a certificate if it thinks fit. A bankrupt may appeal a court's refusal to issue a certificate.

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(48) The Personal Insolvency Task Force was established in 2000 by the Office of the Superintendent of Bankruptcy as part of a government-led review of Canadian insolvency legislation. It issued its final report in August 2002 (note 37).

(49) Ibid., p. 53.

(50) Ipso facto means by the mere act or fact itself.

Chapter 47 repeals section 175 of the BIA. However, Bill C-12 restores section 175 (clause 102).

C. Administrative and Procedural Issues

1. Amendments to the BIA Only

a. Appointment of Interim Receiver (Clauses 13-15 and 96-97)

Under the BIA, the court may appoint a licensed trustee as interim receiver of the property of the debtor in the circumstances specified in sections 46 to 47.1. Section 46 provides that the court may appoint an interim receiver, after the filing of a bankruptcy order, if it is shown to be necessary for the protection of the estate of a debtor. Under section 47, the court may appoint an interim receiver if it is satisfied that a secured creditor has sent, or is about to send, the debtor a notice of intention to enforce its security pursuant to section 244 of the BIA. Finally, under section 47.1, the court may appoint an interim receiver where a notice of intention or a proposal has been filed.

Bill C-12 clarifies that an application for the appointment of interim receiver under sections 46-47.1 must be filed in a court having jurisdiction in the judicial district of the locality of the debtor (clauses 13, 14(3) and 15(3)). The BIA does not currently specify where an application to appoint an interim receiver should be brought.

Under the BIA, the court may order an interim receiver appointed under section 47 or 47.1 to "take such action as the court considers advisable." Chapter 47 removes this broad authority of the court. However, Bill C-12 restores this power (clauses 96 and 97). It also authorizes the court to order an interim receiver to "take conservatory measures" and/or "summarily dispose of property that is perishable or is likely to depreciate rapidly in value" (clauses 14(2) and 15(2)).

Furthermore, Bill C-12 amends provisions of Chapter 47 that limit the duration of an interim receiver's appointment under sections 47 and 47.1. Currently under the BIA, an interim receiver may be appointed under sections 47 or 47.1 "for such term as the court may determine." Chapter 47 proposed to limit the court's authority to set the term of an interim receiver's appointment. Chapter 47 provides that the appointment of the interim receiver under section 47 of the BIA ends on the earlier of the following events:

a. the appointment of a receiver under section 243(2)[(51)] in respect of *any* of the debtor's property;

b. the filing or making of an assignment in bankruptcy;

c. the granting of a bankruptcy order against the debtor;

d. the filing or making of a proposal by or in respect of the debtor;

e. the filing of a notice of intention by the debtor; and

f. the expiry of 60 days after the appointment, or any period specified by the court.

In the case of section 47.1, the appointment ends on the earlier of the following events:

a. the appointment of a receiver under section 243(2) in respect of *any* of the debtor's property;

b. the filing or making of an assignment in bankruptcy;

c. an event that causes a deemed assignment in bankruptcy;

d. the granting of a bankruptcy order against the debtor; and

e. the day on which the court approves the proposal.

Bill C-12 simplifies these provisions, by reducing the number of situations under which the appointment of an interim receiver will be terminated (clauses 14(1) and 15(1)). Under Bill C-12, the appointment of an interim receiver under section 47 or 47.1 ends on the earlier of the following events:

a. the taking of possession by a receiver under section 243(2) *of the property over which the interim receiver was appointed*;

b. the taking of possession by a trustee *of the property over which the interim receiver was appointed*; and

c. the expiry of 30 days after the day on which the interim receiver was appointed, or of any period specified by the court (in the case of an appointment under section 47); or the date of court approval of the proposal (in the case of an appointment under section 47.1).

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(51) Section 243(2) of the BIA provides for the appointment of a receiver pursuant to a security agreement or an order of the court made under any law that provides for or authorizes the appointment of a receiver or receiver-manager.

Thus, a receiver appointed under 243(2) of the BIA, or a trustee, must take possession of the *relevant portion* of the debtor's property in order to be an event that triggers the end of the interim receiver's appointment. In addition, the appointment of the interim receiver is not automatically terminated by the filing of a notice of intention, a proposal, an assignment in bankruptcy, or by an order of bankruptcy.

b. National Receivers (Clause 58)

Section 243(2) of the BIA provides for the appointment of a receiver in two different ways, either pursuant to a security agreement with a creditor or by an order of the court under any provincial or federal law. A receiver takes possession or control of all (or substantially all) of the property that was used in connection with the bankrupt's business. Chapter 47 amends the BIA to provide that only a licensed trustee may be appointed as a receiver under section 243(2). A receiver appointed under section 243 will thus have the authority to act throughout Canada.(52) Chapter 47 also clarifies that the court may only make an order appointing a receiver on the application of a secured creditor.

Clause 58 of Bill C-12 makes a few additional amendments to these provisions. It specifies that the test for appointing a receiver is whether the court "considers it to be just or convenient to do so." Furthermore, Bill C-12 specifies that the court may order a receiver to do any or all of the following: take possession of all or substantially all of the inventory, accounts receivable or other property of the debtor used in relation to the debtor's business; exercise any control that the court considers advisable over the property or over the debtor's business; or take any other action that the court considers to be desirable (section 243(1)).

Bill C-12 also provides that if a secured creditor sends a notice to the debtor of its intention to enforce its security, the court may not appoint a receiver until 10 days after the date the notice is sent – unless the debtor consents to an earlier enforcement of the security, or the court considers it appropriate to appoint a receiver before then (section 243(1.1)).

Bill C-12 also specifies that an application for an appointment of a receiver may only be filed in a court having jurisdiction in the judicial district of the locality of the debtor (section 243(5)).

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(52) Douglas A. Palmateer, "Bankruptcy and Insolvency Reform (2007) – Major Commercial Issues," *Addendum: Practice News and Developments from the Canadian Bar Association*, Business and Corporate Edition, June 2007.

Finally, Bill C-12 provides that if a receiver is appointed by the court, the court may make any order regarding the payment of fees and disbursements of the receiver that it considers to be proper. In particular, the court may make an order giving the receiver a charge over all or part of the property of the debtor, ranking ahead of the claims of the secured creditors – but only if the court is satisfied that the secured creditors who would be materially affected by such an order were given reasonable notice and an opportunity to make representations. Note that the disbursements that may be covered by the order do not include payments made in the operation of the debtor's business (sections 243(6)-(7)).

c. Investment of Trust Funds (Clause 95)

Section 25 of the BIA requires trustees to deposit, in an acceptable financial institution, all moneys received from an estate in a separate trust account for each estate. A trustee cannot withdraw any money from a trust account of an estate without the written permission of the inspectors or the court, except for the payment of dividends and charges that are incidental to the administration of the estate.

Chapter 47 proposed to amend the BIA to allow a trustee to invest trust funds in short-term securities of the federal or provincial government, if the court's permission was obtained and the investments were held in trust for the estate. However, Bill C-12 repeals this amendment (clause 95).

d. Estate Solicitor (Clause 5)

Section 13.4(1) of the BIA prohibits a trustee of an estate from acting for or assisting a creditor of the estate to realize or otherwise deal with the security held by the creditor, unless the trustee has first obtained a written opinion of a legal counsel that the security is valid and enforceable against the estate. Furthermore, the legal counsel must not be acting for the secured creditor.

Chapter 47 amends this provision by requiring that the legal counsel in question not have acted for the secured creditor in the previous two years and not be related to the trustee.

However, Bill C-12 removes these two requirements. Instead, it simply requires that the legal counsel be "independent" (clause 5).

2. Amendments to the CCAA Only: Duties of Monitor (Clause 72)

Chapter 47 introduces provisions into the CCAA to clarify the duties of monitors. Bill C-12 makes a few amendments to these provisions. For instance, it adds a new requirement for monitors to pay a prescribed levy to the Superintendent of Bankruptcy (clause 72, section 23(1)(f.1).

3. Amendments to the BIA and CCAA: Superintendent of Bankruptcy – Compilation of Public Records (Clauses 3 and 73)

Under section 11.1 of the BIA, the Superintendent of Bankruptcy is required to keep a public record of documents such as proposals, bankruptcies and trustee licenses, and must provide information contained in the public record upon request and payment of a prescribed fee. Chapter 47 adds a similar provision to the CCAA (new section 26).

Bill C-12 adds new provisions to the BIA and the CCAA to allow the Superintendent to enter into an agreement to provide a compilation of all or part of the information contained in the public record (clause 3, section 11.1(3) BIA; and clause 73, section 26(3) CCAA).

D. Coordinating Amendments: Treatment of Eligible Financial Contracts (Clause 112)

Eligible financial contracts, commonly known as derivatives, are financial agreements that are used in the security business to hedge against adverse price movements.(53) Eligible financial contracts are accorded special treatment under the BIA and the CCAA. For instance, the restriction on the termination of agreements with a reorganizing debtor under section 65.1 of the BIA does not apply to interest rate swaps or other similar eligible financial contracts, and the netting or setting off of financial obligations between the insolvent person and the other parties to the contract is permitted. Similarly, the stay of proceedings that applies to reorganizations under the CCAA does not apply to eligible financial contracts (section 11.1).

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(53) Frank Bennett, *Bennett on Bankruptcy,* 9th ed., CH, Toronto, 2006, p. 1072.

The definition of "eligible financial contract" in the BIA and CCAA was enacted in 1992.[54] Part 9 of the *Budget Implementation Act, 2007*, which received Royal Assent on 22 June 2007, amends the BIA and the CCAA to enable the Government to prescribe the definition of "eligible financial contract." This will allow the Government to update the definition as financial markets evolve.[55] These amendments have not yet been proclaimed into force. However, on 4 August 2007 the Government released draft regulations, prescribing the definition of "eligible financial contract," which would apply if the amendments are proclaimed into force.[56] (For the time being, the *Budget Implementation Act, 2007* has updated the definition of "eligible financial contract" in the BIA and CCAA. The updated definitions will be repealed if the Government decides to prescribe the definition by regulation.)

The *Budget Implementation Act, 2007* also makes other amendments to the BIA and CCAA to clarify the exemption of eligible financial contracts. For instance, it allows the other parties to eligible financial contracts to seize financial collateral while BIA and CCAA proceedings are ongoing. These amendments came into force on the date of Royal Assent.

Clause 112 ensures that the amendments made by Bill C-12 and Chapter 47 are consistent with the amendments made under the *Budget Implementation Act, 2007* in regards to eligible financial contracts. For instance, subclause 112(10) clarifies that the stay of proceedings that applies in a bankruptcy does not prevent the netting or setting off of compensation of obligations, or any dealing with financial collateral, in respect of an eligible financial contract entered into before the time of bankruptcy. Similarly, subclause 112(23) confirms that the CCAA allows the netting or setting off of compensation of obligations, or any dealing with financial collateral, in respect of an eligible financial contract entered into before proceedings under the Act are commenced. It also provides that an order may not be made under the CCAA if it would have the effect of subordinating financial collateral (clause 112(23), section 34(11) CCAA). Furthermore, clause 112 ensures that Bill C-12 will not override the proposal to define "eligible financial contract" by regulation rather than by legislation.

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(54) Department of Industry, Regulatory Impact Analysis Statement, Eligible Financial Contract General Rules (Companies' Creditors Arrangement Act), *Canada Gazette*, Part I, Vol. 141, No. 43, 4 August 2007.

(55) Ibid.

(56) Eligible Financial Contract General Rules (Bankruptcy and Insolvency Act); and Eligible Financial Contract General Rules (Companies' Creditors Arrangement Act) (Draft Regulations), *Canada Gazette*, Part I, Vol. 141, No. 43, 4 August 2007.

E. Coming Into Force (Clause 113)

The provisions of Bill C-12 come into force on the date of Royal Assent, with the exceptions of clauses 1(1), 1(5)-(7), 3, 6, 9(3), 12, 13, 14(2), 14(3), 15(2), 15(3), 16(2), 16(3), 17(2), 19-22, 25, 31, 34, 35, 37, 42, 44, 46-48, 50, 51(1), 55-57, 58(2) and 67, which come into force on proclamation.

COMMENTARY

Bill C-12 is a long-awaited bill that is intended to correct some of the problems in Chapter 47 of 2005. Although Bill C-12 has been described as a technical amending bill, it is clear that it makes numerous substantive amendments to Canadian bankruptcy and insolvency legislation. These amendments deal with commercial and consumer insolvency issues, as well as administrative and procedural matters under the BIA and CCAA. In combination with Chapter 47, Bill C-12 will introduce wide-ranging reforms to Canadian insolvency legislation. Bill C-12 has not received much public attention, perhaps because of the perception that it has been tabled in order to deal with technical issues.