The Restructuring Review

Fifth Edition

Editor

Christopher Mallon

Law Business Research

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FIFTH EDITION

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EDITOR'S PREFACE

I am very pleased to present this fifth edition of *The Restructuring Review*. As with the previous editions, our intention is to help general counsel, government agencies and private practice lawyers understand the conditions prevailing in the global restructuring market in 2011/2012, and to highlight some of the more significant legal and commercial developments and trends that have been evident in recent years and that are expected to be significant in the future.

Unsurprisingly, the global economy is still struggling to emerge from the worst financial crisis since the Great Depression. The past year has been dominated by uncertainty caused by the economic and sovereign debt crisis in the eurozone, which appears to have had a profoundly unsettling effect on the global economy. We have been reminded powerfully of the impact of excess indebtedness at the governmental, corporate and individual levels, and of the consequences for national balance sheets of the guarantees, whether express or implicit, given by sovereigns to their banking sectors during the financial crisis. The crisis in the eurozone is in many ways a crisis of political leadership and a test of the common bonds within the eurozone as much as an economic crisis, and it is this political angle that has prevented eurozone leaders, until now, from taking the comprehensive and radical action that markets demand to stem the crisis.

In the first half of 2012 global markets have performed badly, and there have been worrying signs of a slowdown in the US and Chinese economies. The performance of these two giant economies was a significant component of the fragile recovery that followed the first phase of the financial crisis, and so a poor outlook in these economies, coupled with the ongoing turmoil in the eurozone, is likely to lead to difficult global economic conditions in the short term. While the picture is continually changing and the only accurate economic prediction that can be made is for more uncertainty in the months ahead, most commentators agree that a significant deleveraging on the individual, corporate and governmental levels is likely to be seen in the coming years and may be an essential prerequisite for a return to stability.

The difficult global economic conditions are widely expected to contribute to a significant increase in restructuring activity in the coming years. As such, this work is becoming ever more relevant and important, in particular because of the international

nature of many corporate restructurings. I would like to extend my gratitude to all the contributors for the support and cooperation they have provided in the preparation of this book, and to our publishers, without whom the completion of this book would not have been possible.

Christopher Mallon
Skadden, Arps, Slate, Meagher & Flom (UK) LLP
London
August 2012

Chapter 3

CANADA

Michael J MacNaughton, James H Szumski and Marc Duchesne[1]

I OVERVIEW OF RECENT RESTRUCTURING AND INSOLVENCY ACTIVITY

Canada's economy weathered the recent global recession better than many. Its banks, unlike many in other jurisdictions, largely avoided the direct impact of the subprime mortgage crisis that gripped the United States. While 2008 and 2009 saw increased levels of insolvency activity, due in large measure to the effect on Canadian exporters of the decline in the US economy, especially in the housing market, 2010 and 2011 were relatively quiet.

In the first quarter of 2012, there are signs that insolvency activity may once again be on the rise in Canada. Based on information available from the Office of the Superintendent of Bankruptcy Canada, Industry Canada, there was a 57 per cent increase in the number of restructuring filings under the Companies' Creditors Arrangement Act[2] ('the CCAA') from the first quarter of 2011 to the first quarter of 2012. The industries most widely affected were manufacturing and real estate, primarily in the provinces of Ontario and British Columbia.

The Bank of Canada, Canada's central bank, anticipates that growth in the Canadian economy will accelerate in the second half of 2012, expanding 2.4 per cent in 2012 and 2013 before moderating to 2.2 per cent in 2014.[3] Nonetheless, sovereign debt concerns in Europe, debt ceilings, unemployment and deficits in the United States, with their effect on exchange rates and export demand, may give rise to uncertainty, particularly given the number of cross-border (US and Canada) enterprises.

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1 Michael J MacNaughton and Marc Duchesne are partners and James H Szumski is an associate at Borden Ladner Gervais LLP.

2 R.S.C., 1985, c. C-36, CCAA.

3 Bank of Canada, Monetary Policy Report (April 2012).

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

Canada is a federation. The Canadian Constitution divides legislative power between the federal or national government and provincial governments. 'Bankruptcy and Insolvency' is a federal head of legislative power.

Secured transactions, corporation law, securities law and similar matters fall primarily within provincial jurisdiction under the 'Property and Civil Rights' head of power. On the other hand, banks and banking are a federal head of power. In addition, federal powers include the incorporation, governance and regulation of federal corporations.

As a matter of constitutional principle, where federal legislation conflicts with provincial legislation the doctrine of 'paramountcy' dictates that provincial legislation must give way to federal legislation. However, the Supreme Court of Canada has held that the doctrine of paramountcy should only be invoked where federal and provincial legislation are clearly contradictory.[4] This is subject to the gloss that there will be cases in which imposing an obligation to comply with provincial legislation would in effect frustrate the purpose of federal law even though it did not entail a direct violation of a federal legislative provision. The fact that a provincial law is incompatible with the purpose of the federal law will also be sufficient to trigger the doctrine of federal paramountcy.[5] Nonetheless, courts will strive to read federal and provincial legislation harmoniously. Subject to the doctrine of paramountcy, provincial legislation will continue to apply notwithstanding the application of federal bankruptcy and insolvency law.

There are three principal federal insolvency statutes in Canada: the Bankruptcy and Insolvency Act ('the BIA'),[6] the CCAA and the Winding-up and Restructuring Act ('the WURA').[7] Limited restructuring proceedings involving both solvent and insolvent companies can also be effected through the federal corporate statute, the Canada Business Corporations Act ('the CBCA').[8]

The BIA is a detailed code running to over 250 sections that provides for voluntary liquidation proceedings, involuntary liquidation proceedings, formal reorganisation proceedings for businesses and individuals, the appointment and regulation of trustees in bankruptcy, the administration of bankruptcy and reorganisation estates, the appointment of receivers or receivers and managers by the court, fraudulent conveyance, preference and similar remedies, the recognition of foreign insolvency proceedings and other matters.

The CCAA is a much shorter statute that provides for court protection for insolvent companies coupled with court supervised formal restructuring proceedings. The CCAA has been used for balance sheet restructurings and operational restructurings, as well as for sales of assets and businesses without a plan of reorganisation.

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4 *Multiple Access v. McCutcheon* [1982] 2 S.C.R. 161.

5 *Canadian Western Bank v. Alberta* [2007] 2 S.C.R. 3, quoted in *Re-Nortel Networks Corp.* (2009), 59 C.B.R. (5th) 23 (Ont. C. A.) at para. 37.

6 R.S.C., 1985, c. B-3, BIA.

7 R.S.C., 1985, c. W-11, WURA.

8 R.S.C., 1985, c. C-44, CBCA.

The WURA was based on the winding-up provisions of the English Companies Act. At one point it was a statute of general application. In some sense it remains a statute of general application, in that it applies or is available for the winding up of many companies that carry on business or have assets in Canada. However, with limited exceptions, its recent use has been primarily restricted to the winding up of regulated financial institutions including banks, trust companies and insurance companies. The WURA now contains special provisions related to the liquidation of regulated financial institutions in conjunction with related federal incorporation, governance and regulatory law.

There are no special bankruptcy or insolvency courts in Canada. Rather, under the BIA,[9] the CCAA[10] and the WURA,[11] jurisdiction to hear matters covered by those statutes is conferred upon the superior courts of each province. Appeals from the superior courts are to the courts of appeal of each province. Appeals from the courts of appeal of the provinces are to the Supreme Court of Canada. Accordingly, the interpretation of insolvency law may differ from province to province.

The explanation of Canadian bankruptcy and insolvency law can be approached in a number of ways. One useful method is to distinguish and explain liquidation and sale processes from restructuring and reorganisation processes. While this distinction is a useful one, it is also somewhat artificial because the CCAA (the restructuring statute of choice for significant cases) and, to a lesser extent, the restructuring provisions of the BIA, may be used to effect sales without a plan or proposal being put to creditors, whether before or after completion of the sale transaction.

Nonetheless, with this critical caveat in mind, Canadian insolvency proceedings can be conveniently divided among:

a liquidating bankruptcies under the BIA;
b liquidation and sale proceedings through court-appointed receiverships;
c proceedings under the CCAA;
d reorganisation proceedings under the BIA; and
e restructuring proceedings under the CBCA.

i Liquidating bankruptcy

A person can become bankrupt under the BIA through a voluntary assignment in bankruptcy; through involuntary creditor-initiated bankruptcy proceedings; or as a consequence of failed reorganisation proceedings under the BIA. To make an assignment in bankruptcy or to take advantage of reorganisation proceedings under the BIA, a person must be an 'insolvent person'. To succeed in an involuntary proceeding, a creditor must prove that the debtor is indebted to the creditor in the amount of at least $1000 and has committed an 'act of bankruptcy'. Insolvency is not a requirement, although most of the acts of bankruptcy enumerated in the BIA are indicative of insolvency.

Upon bankruptcy, all of the property of the debtor is transferred by operation of law to a licensed trustee in bankruptcy and a stay of proceedings arises. Subject to

9 BIA, at s. 183.

10 CCAA, at s. 2 'court'.

11 WURA, at s. 2 'court'.

important exceptions, no creditor has any remedy against the debtor or the debtor's property, or shall commence or continue any action, execution or other proceedings for the recovery of a claim provable in bankruptcy. The most important exception to the automatic stay is that it does not apply to secured creditors. For the most part, secured creditors are free to exercise their rights as secured creditors and to deal with their collateral without reference to or impediment by the bankruptcy proceeding. Most corporate debtors have significant secured debt. Hence, it is not unusual for a bankruptcy to proceed concurrently with or following private secured creditor enforcement or court-appointed receivership proceedings.

Notice of the bankruptcy is given to creditors and published, following which a meeting of creditors is convened. At that first meeting a summary explanation of the causes of the bankruptcy is usually provided, creditors are given a limited opportunity to ask questions, the trustee is affirmed or replaced as trustee of the estate, inspectors are appointed and the meeting is then adjourned. The estate inspectors perform an important governance function in each bankruptcy estate. The trustee in bankruptcy needs inspector approval or court approval in respect of most significant decisions. The estate inspectors, who are usually representatives of creditors, owe a fiduciary duty to the bankruptcy estate.

A trustee in bankruptcy has the power to get in property, sell estate assets, undertake investigations and examine witnesses, undertake litigation, review and contest claims, and distribute assets.

The BIA contains a scheme of priorities.[12] It provides that certain unsecured claims have a preferred status among unsecured claims, and that otherwise, unsecured claims rank ratably. The BIA also provides that certain crown claims (government claims) that would otherwise have the benefit of a statutory deemed trust or lien nonetheless rank as unsecured claims in bankruptcy. The BIA also makes special provision for a limited priority for pension and employee claims as well as certain environmental claims. Because of the scheme of priorities contained in the BIA and the constitutional doctrine of paramountcy (referred to above), courts have held that many provincial legislative priority claims are ineffective in bankruptcy because they conflict with the priority regime contained in the BIA. On the other hand, the BIA scheme of priorities does not apply in receivership proceedings or BIA restructuring proceedings, nor does it apply in non-BIA insolvency proceedings. Accordingly, the timing and choice of insolvency proceedings can have a significant effect on creditor priorities and entitlements.

ii Court-appointed receivership

Since the stay of proceedings that arises on bankruptcy does not apply to secured creditors who are outside the bankruptcy, secured creditors often use different realisation

12 For example, the costs of administration, including the trustee's fees and expenses, rank second in the list of unsecured claims; the trustee's fees and expenses are ranked after secured claims and ahead of most unsecured claims. That means that a trustee in bankruptcy must look to estate assets for recovery unless it has a third-party guarantee.

techniques.[13] Secured creditors typically appoint a receiver in respect of their collateral pursuant to a contractual power, usually contained in their security agreements, or apply to the court for the appointment of a receiver by the court to deal with the collateral as authorised and permitted by the order appointing the receiver.

A secured creditor may apply to a court for the appointment of a receiver or receiver and manager[14] of all or part of the property of a debtor. There are two principal sources of the court's power to appoint a receiver. First, most provincial judicature statutes, recognising the equitable power of a court to appoint a receiver, provide that the court has the power to appoint a receiver where it is just or convenient to do so. The primary exception is the province of Quebec, a civil law jurisdiction, which does not provide for the appointment of receivers. Second, the BIA contains statutory powers permitting the court to appoint a receiver (including an interim receiver) to take possession of the property of an insolvent person used in connection with a business and to exercise control over that property and that business where the court considers it just or convenient to do so.[15]

Where a receiver is appointed (whether under provincial legislation or under the BIA) it acts as a principal in accordance with the directions given to it by the court in the order appointing it and in any subsequent orders. A court-appointed receiver does not take instructions from any creditor. The advantage of a court-appointed receiver or receiver and manager is that its principal actions and activities will be approved by the court. Hence, the prospect of challenges as to the commercial reasonableness of the activities of the receiver are minimised. In addition, since a court-appointed receiver is not the agent of any secured creditor, the exposure of a secured creditor seeking and obtaining the appointment by the court of a receiver or a receiver and manager is reduced (except to the extent that the secured creditor provides a receiver with an indemnity in respect of obligations it incurs in respect of its actions as receiver).

Usually, the focus of a court-appointed receivership is on the sale of the assets of the debtor either as a going concern or piecemeal. Each significant sale will be the subject of an application to the court for approval. In considering a sale, courts will take into account:

a whether the receiver has made a sufficient effort to obtain the best price and has not acted improvidently;
b whether the receiver has considered the interests of all parties;
c the efficacy and integrity of the process by which offers have been obtained; and
d whether there has been any unfairness in the working out of the process.[16]

Stalking horse bidding processes are not uncommon. Credit bidding may also be permitted. The court has the power to vest the assets in a purchaser free of liens and

13 And also because a levy (or tax) applies to all distributions by a trustee in bankruptcy, and so would dilute secured creditor recoveries where secured creditors participated in the bankruptcy.

14 A 'receiver' of property has the powers necessary to dispose of it. A 'receiver and manager' has those powers, as well as the power to carry on the business.

15 BIA, at s. 243.

16 *Royal Bank v. Soundair Corp.* (1991), 7 C.B.R. (3d) 1.

claims, which will instead attach to the proceeds of the sale in the hands of the receiver. On the sale of assets, the proceeds will be held by the receiver to be distributed in accordance with directions provided by the court and in accordance with the respective priorities of claimants.

iii CCAA proceedings

The CCAA allows an insolvent corporation or group of corporations or an income trust (referred to as a 'debtor' or 'debtor companies') to seek court-ordered protection from some or all of its creditors and to attempt to restructure its business and affairs.[17]

To apply for relief under the CCAA a debtor must be a company that (1) is established under Canadian, federal, provincial or territorial law; (2) carries on business in Canada; or (3) has property in Canada, or it must be a trust that has assets in Canada and its units are listed on a stock exchange at the time the CCAA proceeding is commenced (or a majority of the units are owned by a trust that has its units listed on a stock exchange). The debtor must have claims against it and applicable affiliated debtor companies of $5 million or more and must be insolvent,[18] bankrupt or have committed an act of bankruptcy.

Commencement of proceedings and the stay

CCAA proceedings are commenced by an application to the court for an 'initial order'. On the first application and on successive applications, the court has the power to impose broad stays of proceedings against creditors and claimants, including contract counterparties. The court also has the power to grant a stay in respect of many kinds of claims against directors and officers of the debtor. The initial stay of proceedings cannot be for more than 30 days. The stay of proceedings may be extended by subsequent applications and for longer periods.

There are a few statutory restrictions on the stay power. A stay may not prevent a creditor from pursuing a guarantor of the obligations of the debtor (unless the guarantor is also an applicant in the proceedings). The court cannot prevent the beneficiary of a letter of credit from calling on the letter of credit. The court cannot make a stay order that has the effect of compelling a person to extend credit to a debtor after the application is made. A stay order cannot affect the close-out and netting rights of a counterparty to an eligible financial contract.[19]

Appointment of a monitor

In any proceeding under the CCAA a monitor must be appointed. A monitor is similar to a receiver appointed by the court in that it acts as a principal, and owes duties to the court and all persons with an interest in the case. Unlike a receiver appointed by the

17 Creditor-initiated CCAA proceedings are possible but relatively rare.

18 Evidence of a reasonably foreseeable expectation that the debtor will not be able to meet its obligations generally as they fall due may be sufficient to satisfy the test of insolvency for the purposes of the application of the CCAA. See *Re-Stelco Inc.* (2004), 48 CBR (4th) 299.

19 Eligible financial contracts are derivatives contracts.

court, a monitor does not take possession or control of the property or the business of the debtor. Rather, a monitor is entitled to access and information for the purpose of monitoring and reporting on the affairs of the debtor. The duties and powers of a monitor can be adjusted by court order to suit the circumstances of the case, but a monitor has certain minimum statutory responsibilities. Under the CCAA, a monitor is required, among other things, to:

a report to the court on the reasonableness of the debtor's cash-flow statement;

b report to the court on its findings with respect to the state of the debtor's business and financial affairs and the cause of its financial difficulties; and

c advise the court on the reasonableness and fairness of any compromise or arrangement that is proposed between the debtor and its creditors.

Where there is a material adverse change in the business or financial affairs of a debtor, the monitor is obliged to prepare and file a report with the court in connection with that material adverse change. Typically, a monitor will serve and file a report on the status of the debtor, its negotiations with creditors and claimants, and its progress towards a restructuring on virtually every application made by the debtor to the court for any purpose. The monitor has certain reporting and oversight roles prescribed in the CCAA in the event that the debtor wishes to assign or terminate an agreement, or sell or dispose of assets out of the ordinary course of business.

The monitor is not appointed by the debtor and must be independent of the debtor. As restructuring practice has developed, the role of the monitor has come to include assisting the debtor in the restructuring process. Nonetheless, the monitor must act impartially and must consider, communicate with and take into account the interests of all stakeholders in undertaking its role. There is an ongoing debate about the extent, if any, to which a monitor may or should perform the function of financial adviser to the debtor. Some argue that unless a monitor can do so, the process will become more expensive and less efficient because the debtor will need a separate financial adviser. Others argue that to the extent that a monitor performs the role of adviser to the debtor, its independence is compromised and the restructuring process is unbalanced.

On a very practical level, except in very unusual circumstances, the court will regard the monitor as its eyes and ears and will look to the monitor to report in an even-handed and fair way. Virtually any significant step in a case will see the delivery to all parties in interest of a monitor's report to the court. Monitor opposition to a stakeholder position is an enormous obstacle. Monitor support is a powerful advantage.

Use of cash collateral and financing

There is no prohibition on the use of cash collateral in CCAA proceedings. A debtor may continue to use its cash, accounts receivable and other property in the ordinary course without the need for a cash collateral order. The usual stay of proceedings in the initial CCAA order prohibits action by creditors but leaves the debtor free to use its property in the ordinary course.

If financing is required, the court in a CCAA case has the power to authorise it upon notice to secured creditors who are likely to be affected. Typically, financing is authorised with the benefit of a court-ordered charge upon all of the debtor's property. The ranking of the court-ordered charge is in the discretion of the court but typically

ranks in priority to all pre-filing claims and charges. In deciding whether to make an order granting such a charge, the court is to consider, among other things:

a the period during which the company is expected to be subject to CCAA proceedings;

b how the company's business and financial affairs are to be managed during the proceedings;

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

d whether the financing would enhance the prospects of a viable compromise or arrangement being made; and

e whether any creditor would be materially prejudiced as a result of the court-ordered charge.

While not required and within the discretion of the court, every initial CCAA order will contain a court-ordered charge upon all of the debtor's property securing the fees and expenses of the monitor, the monitor's counsel and the debtor's counsel. The court may also grant a charge with respect to the fees and expenses of any financial or other experts retained by the debtor or the monitor, and the fees and expenses of any financial, legal or other experts engaged by any other interested person if the court is satisfied that the security or charge is necessary for their effective participation in the CCAA proceedings.

The court has the authority to grant a charge upon all of the debtor's property in favour of the debtor's directors and officers as indemnification against obligations and liabilities that they may incur as a director or officer of the company after the commencement of the CCAA proceeding. Such a charge is typically found in the initial CCAA order, and it is regarded as an appropriate protection to induce directors to continue in office. The ranking of the D&O charge is a matter of negotiation; there is no hard and fast rule. For the court to grant the D&O charge, it has to be convinced that the debtor could not obtain adequate indemnification insurance for the directors or officers at a reasonable cost.

Contract rejection

A debtor has the ability to reject or repudiate any agreement (with certain exceptions) to which the company is a party at the commencement of the CCAA proceeding with or without a court order. To do so without a court order, the debtor must provide notice of its intent to reject or repudiate the agreement to the other parties to the agreement and the monitor, and the monitor must approve of the rejection. The agreement is rejected if the parties to the agreement do not object within 30 days after receiving notice. If the debtor wishes to reject a contract and the monitor does not approve of the rejection, the debtor may apply to the court for an order that the contract be rejected. Parties to the agreement to be rejected may apply to a court for an order that the agreement not be rejected. In considering whether to grant an order either rejecting a contract or that a contract not be rejected, the court is to consider, among other things, whether the monitor approved the proposed rejection; whether the rejection would enhance the prospects of a viable compromise or arrangement being made in respect of the debtor; and whether rejection would likely cause significant financial hardship to a party to the agreement. If an agreement is rejected, a party to the agreement who suffers a loss in relation to the rejection is considered to have a provable claim in the CCAA proceedings.

There are certain agreements that cannot be rejected under the CCAA (eligible financial contracts, collective agreements, financing agreements if the company is the borrower, and a lease of real property or of an immoveable if the debtor is the lessor). Additionally, if the debtor has granted a right to use intellectual property to a party to an agreement, any rejection of the agreement does not affect that party's right to use the intellectual property — including its right to enforce exclusive use — during the term of the agreement, including any period for which the party extends the agreement as of right, as long as the party continues to perform its obligations under the agreement in relation to the use of the intellectual property.

A stay under the CCAA usually prohibits creditors from terminating contracts with the debtor (other than eligible financial contracts).

Asset sales

Sales of assets, especially non-core assets, can be a critical element of the restructuring of a business. Where material dispositions of assets are contemplated, court approval will be required. In the case of material asset dispositions, a disposition strategy and marketing plan will almost invariably be discussed first with the monitor. Thereafter an application will be made to the court for approval of the disposition strategy. On the completion of the disposition process but before completion of a transaction, a motion for approval of the particular sale usually will be made to the court. (If the assets are not material or are only marginally so, this process can be reduced or eliminated.) This process is similar to the use of Section 363 of the Bankruptcy Code to effect sales in a Chapter 11 case. (As a result of the number of cross-border cases, stalking horse and auction sales are becoming more common in Canada.) From a purchaser's perspective, an acquisition through a CCAA proceeding can be attractive because the court has the power to convey title to property on a relatively risk-free basis.

How a sales process will be managed varies from case to case. Options include:

a leaving the debtor to run the process;

b leaving the debtor to run the process subject to monitor oversight and DIP lender (and perhaps other secured creditor) approval at specified milestones;

c authorising the monitor to run the process; or

d engaging an investment bank or similar person to run the process.

Of course, variations and combinations are possible.

Creditors, claims and classification

Where a plan is developed it must be put before the creditors for approval. It is usual, but not necessary, to put a plan or arrangement to all creditors.

Where a debtor determines to put a proposal or plan to some or all of its creditors, a mechanism must be put in place for the proof of the claims of creditors to be filed and considered. This is usually effected through what has come to be known as a 'claims procedure'. A claims procedure is a procedure that is approved by the court that sets out when and how creditors must file their claims, and how disputes between the debtor and the claimant about the validity and quantum of claims will be resolved. There may be separate claims processes for determining the validity and quantum of claims for voting purposes and for distribution or participation purposes. The process for valuing claims

for voting purposes is often simpler than the process for valuing claims for distribution purposes. A simpler process of valuation for voting purposes is often adopted in the interest of accelerating the restructuring process.

A debtor may divide its creditors into classes in connection with creditor meetings to be held to consider a restructuring plan. The debtor is required to obtain court approval of the classification before any creditor meetings are held. The CCAA provides that creditors may be included in the same class if their interests or rights are sufficiently similar to give them a commonality of interest, taking into account:

a the nature of the debts, liabilities or obligations giving rise to their claims;

b the nature and rank of any security in respect of their claims; and

c the remedies available to the creditors in the absence of the restructuring plan being sanctioned, and the extent to which the creditors would recover their claims by exercising those remedies.

The plan is a contract that binds all those who are affected by its terms, but only to the extent that an affected class approves the 'offer' to that class by the requisite majority. This means that any range of options agreeable to the debtor and its creditors is permissible (e.g., debt forgiveness, debt conversion, debt restructuring). There is considerable law for the proposition that while commonality of interest should determine classification questions, the courts will approach such questions with 'non-fragmentation' in mind; that is, courts will not favour a multiplicity of classes, as that will lead to fragmentation and is more likely to result in plan failure.

Each class of creditors must approve any plan put to it by separate vote. Creditor approval requires a double majority: a majority in number of creditors voting (a 'headcount' majority) and a two-thirds majority in value of the claims voting (a 'value' majority).

There is no provision for cramdown in the CCAA. All classes of creditors voting must approve any plan put forward. However, as the CCAA is premised on insolvency, equity holders do not have a blocking position.

Companion equity arrangements

CCAA proceedings are often combined with reorganisations or arrangements under the corporate statutes applicable to the debtor. Through those mechanisms, debt-for-equity swaps can be effected, existing equity rights can be altered or eliminated and other corporate changes can be effected.

Court approval

Creditor approval of a restructuring plan is not a sufficient condition. Approval of a plan by the court is also required.

Where the creditors have approved a plan by the statutory majorities the debtor will apply to the court for approval of the arrangement. Courts have often said that they are not a 'rubber stamp', and will look critically at the plan and the process that has been followed before granting approval and sanctioning a plan.

The court applies two tests: first, whether the statutory requirements of the CCAA have been met, and second, if they have, whether the plan is fair and reasonable. If a plan

has been approved by a significant majority of creditors it is highly unlikely that a court would intervene to overturn the decision of the creditors.

iv Reorganisation proceedings under the BIA (proposals)

Part III of the BIA governs formal debtor-initiated restructuring proceedings initiated by the filing of a proposal or a notice of intention to make a proposal under the BIA. Part III of the BIA is one of the three basic options for formal restructuring proceedings in Canada. A formal restructuring may also be effected under the CCAA or under the arrangement provisions of the CBCA.

While a bit of an oversimplification, Part III of the BIA is most commonly employed in the restructuring of small to medium-sized businesses. The CCAA is more commonly used in respect of larger and more complex proceedings, including cross-border cases.[20] The CBCA has been used to restructure public debt, usually on a pre-packaged basis.

Under the BIA an insolvent person may file a notice of intention to make a proposal or a proposal. A proposal is a formal plan presented to unsecured creditors. A notice of intention is an administrative filing giving rise to a stay of proceedings affording a corporate debtor time to file a proposal. Either filing is an administrative step that effects an automatic stay of proceedings against all of the corporate debtor's creditors, secured and unsecured. The theory behind the proposal provisions of the BIA is that a business restructuring is to be preferred over a liquidation. Where a notice of intention to make a proposal or a proposal is filed, a licensed trustee in bankruptcy must agree to act in connection with the proceedings, will have obligations to monitor and report on the proceedings, and typically will assist the debtor in negotiating with creditors and formulating a proposal to put to creditors.

In order to succeed, a BIA proposal must be approved by a double majority of unsecured creditors (a bare majority of unsecured creditors voting and two-thirds in value of unsecured creditors voting). A proposal need not be made to secured creditors. Where a proposal is also made to secured creditors, the proposal must obtain that same double majority in respect of each class of secured creditors to whom the proposal is made. Accordingly, classification issues can arise. Typically in small to medium-sized proposal situations, the corporate debtor will seek the support of its primary secured creditor for the proposal and will not often make a proposal to that secured creditor as the secured creditor usually will have an effective veto that, if exercised, will allow the secured creditor to invoke its ordinary rights as a secured creditor. In addition, the BIA provides an opportunity for creditors to seek relief from the automatic stay of proceedings and to seek the appointment of a receiver or receiver and manager, among other things.

A notice of intention to make a proposal or proposal process may be combined with the appointment of a receiver to effect a sale as a going concern.

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20 In general terms, anything that can be done under the CCAA can also be done under Part III of the BIA. Having said that, the CCAA permits greater flexibility, tailoring and fine-tuning than Part III of the BIA.

v Plans of arrangement under the CBCA

Corporations subject to the CBCA[21] may carry out fundamental corporate changes, such as mergers, acquisitions, reorganisations and other transactions, through a plan of arrangement. Plans of arrangement are very flexible and allow multiple steps and transactions to be accomplished in one statutory procedure.

In the past few years, the CBCA arrangement provisions have been successfully used to effect amendments in respect of debt obligations and debt-to-equity conversions. Where a balance sheet restructuring is required, asset sales are not necessary and there is no need to address non-public debt (and especially where the majority of public debt-holders are supportive and have committed to a restructuring), a CBCA plan of arrangement may be a faster, cheaper and generally more efficient process than a CCAA proceeding.

vi Common issues in insolvency proceedings

Treatment of contracts in bankruptcy

The rules that apply to contracts in insolvency differ among Canadian insolvency regimes. In some cases contracts may be rejected, or they may be assigned to purchasers notwithstanding no-assignment clauses. In other cases, contract counterparties may be stayed from terminating contracts as a consequence of insolvency or bankruptcy.

In a liquidating bankruptcy, a trustee in bankruptcy may apply to the court for an order compelling the assignment of a contract notwithstanding that the contract provides that it may not be assigned without the consent of the counterparty. Similar relief is available under the CCAA or in Part III BIA proposal proceedings, but likely not in receivership proceedings under the BIA. Where a court-ordered assignment is available the court has a relatively broad discretion whether to approve the assignment or not. Court-ordered assignment of certain categories of contracts is prohibited. Post-filing contracts, eligible financial contracts and collective agreements are not assignable.

Counterparty termination rights triggered by insolvency or bankruptcy are stayed in CCAA proceedings and in proceedings under Part III of the BIA. They may be stayed by the terms of a court-appointed receivership order. They likely are not stayed in a liquidating bankruptcy.

The disclaimer or rejection of contracts is authorised in CCAA proceedings and in proceedings under Part III of the BIA. A debtor may reject a contract with the consent of the monitor or the proposal trustee subject to the right of any party to the contract to move before the court for an order that the debtor should not be permitted to reject the contract. If the monitor or proposal trustee does not consent to the contract rejection, the debtor may move before the court on notice to all parties to the contract for an order permitting the rejection of the contract. Certain categories of contracts may not be rejected: an eligible financial contract, a collective agreement, a financing agreement if

21 A CBCA corporation is a corporation established or continued under the CBCA. Many Canadian companies are established or have been continued under provincial corporation statutes. The CBCA arrangement provisions will not apply to them unless they are first continued under the CBCA.

the debtor is the borrower and a lease of real property if the debtor is the lessor. A court-appointed receiver does not have a statutory right to reject a contract made by the debtor in receivership. A trustee in bankruptcy in a liquidating bankruptcy does not have the statutory right to reject a contract made by the bankrupt but appears to have a 'common law' right to do so.

Where the BIA and the CCAA permit contract rejection, there are special protections for licensees of intellectual property. While a licensor may reject a licence, the licensee continues to be entitled to use the intellectual property during the term of the licence agreement provided the licensee continues to perform its obligations under the licence agreement in relation to the use of the intellectual property.

Security interests

Security interests in personal property are dealt with by provincial personal property security statutes. These statutes govern the creation of security interests, the perfection of security interests, the priority of security interests among one another and against certain other kinds of claims, as well as the registration and enforcement of security interests. Security interests in real property are governed by provincial real property statutes concerning title and registration in respect of real property interests, as well as the enforcement of mortgages and charges against real property. (Construction lien or builders lien law is also a matter of provincial jurisdiction.)

Clawback actions

The preference and transaction at undervalue provisions of the BIA apply in liquidating bankruptcies, proposal proceedings under Part III of the BIA and in proceedings under the CCAA. However, if the plan or proposal under the CCAA or the BIA put forward and accepted by creditors and approved by the court stipulates that those provisions do not apply then they will not apply.

Under Section 95 of the BIA, a transfer of property, provision of services, charge on property or payment made in favour of an arm's-length creditor with the intent to prefer that creditor over others is voidable if it occurred within three months before the date of the initial bankruptcy event. Where the debtor and the creditor are not at arm's length, the review period is 12 months rather than three months. If the payment or other disposition in question had the effect of preferring the creditor then intent to prefer is presumed, although it may be rebutted.

The court may grant relief in respect of a transaction in which the consideration received by the debtor is nothing or is conspicuously less than the fair market value of the consideration given by the debtor. The remedy is wide-ranging. The court may declare the transaction void. The court may grant a money judgment against the counterparty or any person privy to the transaction. Where the debtor is at arm's length from the transferee, the review period is one year from the date of the initial bankruptcy event. In that case, in order to succeed, it must be proved that the debtor was insolvent at the time of the transaction or was rendered insolvent by the transaction, and also that the debtor intended to defraud, defeat or delay any creditor. Where the debtor is not at arm's length from the transferee and the transaction occurred within one year before the date of the initial bankruptcy event, all that must be proved is that the parties were not at arm's length and that there was a conspicuous difference between the value of

the consideration given and received. Where the debtor is not at arm's length from the transferee and the transaction occurred more than one year before the date of the initial bankruptcy event but less than five years before the date of the initial bankruptcy event, a remedy may be available. In addition to proving that the parties were not at arm's length and that there was a conspicuous difference in the value of the consideration given and received, it must also be proved that either the debtor was insolvent at the time of the disposition or was rendered insolvent by the disposition, or that the debtor intended to defraud, defeat or delay a creditor.

In addition to the statutory remedies available under the BIA, most provinces have enacted fraudulent conveyance and preference statutes that are available to trustees and should be available to other creditor representatives in insolvencies. It is also important to note that the wide-ranging oppression remedy under the CBCA and other corporate statutes may also be available to trustees and other creditor representatives.

III SIGNIFICANT TRANSACTIONS AND KEY DEVELOPMENTS

There have been a number of significant developments in Canadian insolvency law and practice over the last two years. Of particular note are recent developments concerning the continuing disharmony between reorganisation and liquidation regimes, particularly in the context of pension priority regimes; the availability of DIP financing for purposes other than facilitating a compromise or arrangement with creditors; and the status of environmental remediation orders against debtors who have obtained protection under the CCAA.

i Pension priorities

Many provincial statutes create liens, trusts or other priority rights that do or may conflict with priority rights created by federal insolvency law. Sometimes the conflict is stark and unavoidable. For example, some provincial priority rights conflict with the scheme of priorities set out in the BIA. In those cases the result of the conflict is often clear: the provincial priority must give way to the federal regime as a consequence of federal law's constitutional paramountcy in the event of a conflict. Sometimes the conflict seems less clear. Sometimes there is disagreement about whether or not there is a conflict.

It is relatively clear that under the CCAA the court has the power to create a court-ordered charge in favour of a DIP lender, which ranks in priority to priority charges created by provincial law, including 'deemed trusts'. It is also relatively clear that in the event of the bankruptcy of a debtor, those deemed trusts will fail. There is a debate about whether such deemed trusts are effective in a CCAA context. It is clear that they may be subordinated by court order. Creditors and debtors and their advisers have often promoted CCAA filings with a two-track process. One track is the pursuit of a going concern sale of the business, sometimes through a stalking horse process. The other track (often more speculative) is the pursuit of a reorganisation with creditor votes and court approval. In the past, creditors have supported this approach. It preserves options, and if a sale is achieved without a plan, the debtor company will often be placed into bankruptcy where the usual bankruptcy priorities will apply and many statutory priority claims may be avoided. The Supreme Court of Canada has said that the CCAA and the

liquidation regime under the BIA should not be treated as distinct regimes subject to a temporal gap between the two.[22] The two statutes are related, and no gap exists between them that would allow the enforcement of property interests at the conclusion of the CCAA proceedings that would be lost in bankruptcy.[23]

Recently, the Ontario Court of Appeal reached a different conclusion. In *Re Indalex*,[24] the debtor company, with the assistance of the monitor and its US parent, had conducted a joint sales process under the CCAA and pursuant to Section 363 of the US Bankruptcy Code. The Canadian debtor had two registered pension plans. At the time the CCAA proceedings were commenced, one of the plans was in wind up and it was anticipated that the second plan would be placed in wind up at some point. Both plans had solvency deficiencies. In a court-supervised liquidation (bankruptcy or receivership) under the BIA, unpaid current service pension contributions as well as any solvency deficiency claims would rank as unsecured claims, subject to a statutory priority for pre-receivership or pre-bankruptcy normal unpaid pension contributions. In *Indalex*, pension claimants and the pension regulator argued that the deemed trust priority for unpaid pension contributions continued to apply notwithstanding the commencement of CCAA proceedings; and the deemed trust extended not only to unpaid current service contributions but also to the solvency deficiency on plan wind up. If these two propositions are correct, then secured creditors face the risk that, in permitting or supporting CCAA proceedings, their claims may be subordinated to very substantial pension claims. Pension claimants also argued that their argued-for pension priority claims could not or should not be subordinated to post-filing priority DIP financing.

The Ontario Court of Appeal concluded that while courts have the jurisdiction to grant charges with priority status over a pension plan deemed trust, they should do so on a case-by-case basis, and only after determining that the application of the provincial deemed trust legislation would frustrate the debtor's ability to restructure and avoid bankruptcy. The Court further concluded that the Canadian debtor, as administrator of the two pension plans, was a fiduciary in respect of the plans, and should have taken steps to see the deficiency claims satisfied and pensioners protected as part of the CCAA sales process. In the circumstances, the deemed trust in respect of the pension plan in wind up should therefore be enforced and, as a consequence of the breach of fiduciary duty, equivalent relief should be given in respect of the plan that was not in wind up. The relief granted was described as the imposition of a constructive trust. It might also be analogised to the application of the doctrine of equitable subordination. In any event, the treatment and priority of these deficiency claims in a CCAA proceeding appears to be fundamentally different than would be the case in bankruptcy.[25]

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22 *Re Ted Leroy Trucking Ltd.* (2010), 72 C.B.R. (5th) 170 at para. 78.

23 See *Re Ivaco* (2006), 83 O.R. (3d) 108 (Ont. C.A.) referred to in *Re Ted Leroy* at para. 78.

24 (2011), 75 C.B.R. (5th) 19.

25 Leave to appeal the Ontario Court of Appeal's decision in *Re Indalex* to the Supreme Court of Canada has been granted. The appeal was heard by the Supreme Court of Canada on 6 June 2012, and is under reserve.

Several decisions since *Indalex* have limited its application in other insolvency contexts. In *Re Timminco Ltd.*[26] the Ontario Superior Court of Justice granted priority charges in a CCAA proceeding to secure the fees and expenses of the financial advisers of the debtor, an indemnity for the officers and directors of the debtor, and DIP financing to fund the restructuring. Building on *Indalex*, the Court determined that it would frustrate the restructuring and the ability of the debtor companies to restructure if the charges were not given priority over pension plan deemed trust claims. Among other things, the Court was persuaded by evidence that:

a notice of the application for priority charges had been given to all affected pension entities;

b without the priming charges, a restructuring would be unable to proceed and the debtor would likely become bankrupt;

c the DIP financing and the services of the financial advisers, officers and directors of the debtor would not be available absent a priming charge;

d the terms of the DIP financing were at market or otherwise appropriate; and

e the charges were supported by the court-appointed monitor.

The Court was also satisfied that the debtor companies were not in breach of their fiduciary duties with respect to the pension plans, as the pension liability that was to be primed would have had no priority in the bankruptcy proceedings that would inevitably ensue if the priority charges were not granted.

In *Re White Birch Paper Holding Co.*[27] the Quebec Superior Court also considered *Indalex* in the context of an application for a priority charge to secure DIP financing that would rank in priority to pension plan deemed trust claims. As in *Timminco*, the Court was satisfied that if the requested charge was not granted, bankruptcy would be inevitable. However, the Court went on to conclude that the reasoning in *Indalex* is inapplicable in the province of Quebec due to differences between provincial pension statutes. Following an earlier decision of the Supreme Court of Canada, the Court concluded that the only statutory deemed trusts that are valid under the CCAA are those specifically mentioned in the statute. This does not include pension plan deemed trusts under provincial legislation. Furthermore, in *White Birch* the debtor company was not the administrator of the pension plans and therefore did not act in breach of any fiduciary obligations that might otherwise have formed the basis for equitable relief.

The decisions in *Timminco* and *White Birch* demonstrate that courts will still grant priority charges that prime pension plan deemed trust claims, provided that appropriate notice is given and that the court is satisfied the priority charges are necessary to permit a restructuring of the debtor company. These decisions do not assist with the question of whether pension plan deemed trust claims trump pre-filing security interests for distribution purposes under the CCAA, nor do they address the apparent disharmony that *Indalex* has created between the treatment of pension claims in bankruptcy and under the CCAA. These questions may be answered when the Supreme Court of Canada

26 (2012), 86 C.B.R. (5th) 171.

27 (2012), CarswellQue 3901.

delivers its reasons in connection with an appeal of the *Indalex* decision, which was heard in June 2012.

ii DIP financing for purposes other than facilitating a compromise

Courts have generally approved DIP financing for debtors in CCAA proceedings where the court is satisfied that the financing will improve the prospect of a viable compromise or arrangement being made in respect of the company. DIP financing has also been extended in certain circumstances to fund a sale of all or part of a debtor's business through a CCAA process. A recent decision of the Ontario Court of Appeal in *Re Crystallex*[28] addresses the possible scope of DIP financing and its permitted purposes.

Crystallex is a Canadian mining company that acquired the right to develop a gold project in Venezuela through Corporacion Venezolana de Guayana, a state-owned Venezuelan corporation. Before project development could begin, a contractual dispute developed and those development rights were unilaterally rescinded. Crystallex began arbitration proceedings against the government of Venezuela, claiming compensation of $3.4 billion for the loss of its investment.

As a consequence of the contractual dispute, Crystallex was unable to pay its debts as they became due. Its only assets consisted of $10 million of equipment, $2 million of cash and the arbitration claim. Its principal liabilities included $100 million in senior unsecured notes due and payable on 23 December 2011, and other liabilities of $1.2 million and $8 million, respectively. Crystallex therefore sought and obtained protection from its creditors under the CCAA.

In the CCAA proceedings, Crystallex applied for court approval of DIP financing in the amount of $36 million, with a term of three-and-a-half years. The purpose of the DIP financing was to fully fund the company's ongoing legal and administrative expenses until the arbitration claim was resolved. The terms of the DIP financing included significant governance rights in favour of the DIP lender, and provided the DIP lender with a significant share in the proceeds of the arbitration claim, if successful. Crystallex informed the court that if the arbitration claim was successful, it was likely that all of the creditors would be paid in full.

Virtually all of Crystallex's creditors opposed approval of the proposed DIP financing. They argued that the DIP financing exceeded what was necessary to complete a compromise or arrangement with creditors. In effect, the terms of the proposed DIP financing coupled with the CCAA stay of proceedings would bind the creditors to passive participation in the arbitration litigation over the next three-and-a-half years and would give significant control, and a share in the upside, of the arbitration to an unrelated third party, all without the benefit of a creditor vote and with no ability for the creditors to enforce their rights as such against the debtor company. The noteholders proposed an alternative DIP financing arrangement that would provide Crystallex with $10 million over a six-month period, with the possibility of negotiating further extensions if Crystallex required additional financing to complete negotiation of a compromise with the noteholders.

28 [2012] O.N.C.A. 404.

Canadian case law had previously provided that DIP financing should not be authorised to permit a debtor company to pursue a restructuring plan that does not involve an arrangement or compromise with creditors. In *Cliffs Over Maple Bay*,[29] the British Columbia Court of Appeal overturned an order approving DIP financing for a real estate development company in CCAA proceedings. The debtor had proposed to use the financing to complete the development of a major real estate project over a lengthy period of time, while remaining under the protection of the CCAA, and to use the proceeds of sale of the completed project to repay its obligations at some future date.

Notwithstanding *Cliffs Over Maple Bay*, the Ontario Superior Court of Justice approved the DIP financing proposal put forward by Crystallex. On appeal to the Ontario Court of Appeal, the lower court decision was affirmed. The courts distinguished *Cliffs Over Maple Bay* on the basis that although Crystallex had originally expressed an intention to stay creditor claims until the arbitration was resolved, its more recent evidence was that it was prepared to negotiate a plan of compromise with its creditors. The courts also rejected the argument that the DIP financing was in effect a plan of compromise without a creditor vote, noting that although the DIP financing affected the noteholders' leverage in negotiating a plan and had made negotiation of a plan more complex, it had not compromised the terms of the company's indebtedness or taken away any of the noteholders' legal rights.

The result in *Crystallex* is unusual. It blurs the line between DIP financing and exit financing by approving DIP financing in an amount and for a time period that exceeds the debtor's restructuring needs. More generally, it raises questions about what a debtor company may do without seeking the approval of its proposed actions by its creditors as part of a plan. There is no question but that sales of all or part of a debtor's business may be effected with court approval, on notice to creditors but without the need for a plan. There is authority for the proposition that in certain cases a debtor may enter into settlement agreements with some creditors with court approval, on notice to creditors but without the need for a plan. *Crystallex* seems to stand for the proposition that at least in some cases a debtor may part with a significant stake or interest in its business with court approval, on notice to creditors but without the need for a plan and even over the objection of virtually all of the debtor company's creditors.

iii Environmental claims

Many Canadian provinces have enacted legislation for the protection of the environment. These statutes provide government regulators with the power to order present and former owners of contaminated property to undertake environmental remediation. If the owners refuse to comply, government regulators may undertake such environmental remediation on their own accord and seek compensation from those responsible for the property.

From a constitutional perspective, regulation of the environment is a provincial head of power. However, the CCAA includes limited carveouts and protections related to the environment. Monitors are protected from personal liability under environmental

29 (2008), 46 C.B.R. (5th) 7.

remediation orders.[30] Compensation claims for remediation costs incurred by a province or by Her Majesty in right of Canada are entitled to a super-priority charge over the affected property.[31] Such compensation claims are also 'claims' against the person responsible for the property, which may be addressed through claims procedures established under the CCAA.[32] Finally, subject to the limited discretion of the court, the stay of proceedings in a CCAA restructuring does not apply to an investigation or proceeding commenced by a regulatory body, including an environmental regulator, other than with respect to the enforcement of a payment ordered by the regulatory body or the court.[33]

On the one hand, many environmental remediation orders create performance obligations that do not require a debtor company to make a payment. Such orders would appear on their face to be exempt from the CCAA stay of proceedings. On the other hand, by requiring a debtor company to incur costs in connection with environmental contamination, such orders may have the effect of imposing a pecuniary obligation on the debtor with respect to matters that arose before the filing date, contrary to the restructuring philosophy of the CCAA. This interplay between insolvency law and environmental law has been the subject of considerable scrutiny in two recent restructurings: *Re AbitibiBowater Inc.*[34] and *Re Nortel Networks Corp*.[35]

Abitibi was one of the world's largest publicly traded pulp and paper manufacturers. Among Abitibi's assets was real property located in the province of Newfoundland, where Abitibi operated several industrial facilities. By 2008, the operation of these facilities had either ceased or the facilities were in the process of being closed. Before the final facility could be closed, the province passed legislation to authorise the expropriation of a substantial portion of Abitibi's assets in Newfoundland, including much of its real property.

In 2009, Abitibi encountered financial difficulties and filed for insolvency protection under the CCAA. A claims process was conducted and creditors were required to prove their claims by a particular date. The province did not prove any claims. After the claims bar date, however, the province issued a number of environmental remediation orders against Abitibi. The orders would have required Abitibi to expend significant time and money to cure environmental contamination on properties in Newfoundland that Abitibi no longer had an interest in. Abitibi took the position that the orders were 'claims' that were now barred as a consequence of the claims bar order. The province took the position that the remedial orders created performance obligations rather than monetary obligations and were therefore not caught by the claims process.

The Court concluded that the orders were monetary in nature, and therefore the province should have filed a proof of claim in the claims process. Having failed to do so, the province was barred from enforcing the orders. In reaching this conclusion, the Court

30 CCAA, at ss. 11.8(3), (5) and (7).

31 CCAA, at s. 11.8(8).

32 CCAA, at s. 11.8(9).

33 CCAA, at s. 11.1.

34 (2010), 68 C.B.R. (5th) 1.

35 (2012), 88 C.B.R. (5th) 111.

analysed the pith and substance of the orders. It noted that the orders required Abitibi to expend time and money to remedy pre-filing environmental damage to real property that had been expropriated. All of the benefits of the remedial work would in fact accrue to the province, which had expropriated the property before the commencement of the CCAA proceedings. Furthermore, the timelines established in the orders were unrealistic. In the Court's view, the province likely did not intend that the remedial work would be performed by Abitibi, but rather that the province would undertake the remediation work after Abitibi failed to do so and would then assert a monetary compensation claim against Abitibi.

A similar issue was addressed by the Ontario Superior Court of Justice in *Re Nortel Networks Corp*. Nortel encountered financial difficulty and sought protection under the CCAA. A claims process was authorised by the Court and the creditors were required to prove their claims. Nortel owned real property at a number of sites in the province of Ontario, where it had at one time operated industrial facilities. Prior to the commencement of the CCAA proceedings, those operations were shut down. After the commencement of the CCAA proceedings, the Ontario Ministry of the Environment issued an order and prepared a number of further draft orders that would have required Nortel to expend time and money to remedy environmental damage to the properties.

Nortel applied to the court for relief, asserting that the orders were monetary claims that ought to be addressed through the claims process. The Ministry defended the orders, arguing that unlike *AbitibiBowater*, Nortel continued to own the property, such that no benefit would accrue to the Ministry; the Ministry had not undertaken any of the remediation work on its own, and was not seeking compensation for its costs in that regard; and it was too speculative and remote to determine whether any such remediation work would be performed by the Ministry.

The Court concluded that the environmental orders were monetary in nature, and should therefore be addressed through the claims process. The Court was of the view that although regulators are generally unaffected by the CCAA stay of proceedings, once a regulator takes steps that require the debtor company to take actions in respect of a factual matrix that arose prior to the filing date, if those actions require a monetary expenditure they are claims to be addressed through the claims process and they are affected by the CCAA stay.

The foregoing decisions would appear to leave little room for environmental regulators to manoeuvre in CCAA restructuring proceedings. While regulators are free to conduct their own investigations they cannot take steps that would require the insolvent debtor to incur costs with respect to pre-filing environmental damage. Leave to appeal the decision of the Court in *AbitibiBowater* was denied by the Quebec Court of Appeal, but has been granted by the Supreme Court of Canada.[36] Similarly, leave to appeal to the Ontario Court of Appeal has been sought and granted in *Nortel Networks Corp*. It

36 The appeal on the merits was heard by the Supreme Court of Canada in November 2011 and is under reserve.

is therefore likely that the status of environmental remediation orders in Canada will continue to evolve over the coming year.

IV INTERNATIONAL ISSUES

The CCAA permits applications for the recognition of foreign proceedings. The recognition of foreign proceedings under the CCAA requires the court to identity whether the proceeding is a 'foreign main proceeding' or a 'foreign non-main proceeding'. A foreign main proceeding is a proceeding that is taken in the jurisdiction where the debtor has the centre of its main interests (deemed to be the company's registered office unless there is proof to the contrary). A foreign non-main proceeding is any proceeding other than a foreign main proceeding.

If a recognition order is granted in connection with a foreign main proceeding, the court is required to make an order, subject to any terms and conditions it considers appropriate, staying proceedings against the debtor and prohibiting the debtor from selling its property in Canada outside the ordinary course of business. With respect to a foreign non-main proceeding, it is within the court's discretion to grant such orders. The court also has the authority, in the case of a foreign main proceeding and a foreign non-main proceeding, to make any order that it considers appropriate if the court is satisfied that it is necessary for the protection of the debtor's property or the interests of a creditor or creditors. Such orders may include examination of witnesses and authorising the monitoring of the debtor's business and financial affairs in Canada for the purpose of reorganisation.

Courts in Canada have given great weight to public policy in favour of the coordination of international insolvencies when considering applications pursuant to the CCAA. Canadian courts expect that they and local stakeholders will be informed of important developments in the foreign proceedings. To that end, it has become usual for the court to appoint a person (often a licensed trustee in bankruptcy) as an 'information officer' with access to the books, records and property of the applicants, and with the power and the responsibility to report to the court and to Canadian stakeholders upon material developments in the foreign proceedings, including the filing of a plan or significant dispositions of assets.

Appendix 1

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Marc Duchesne is partner at Borden Ladner Gervais LLP and head of their Quebec Financial Services Group. Mr Duchesne is a graduate of the University of Ottawa and was admitted to the Quebec Bar in 1981. He acts as a solicitor and litigator in banking, bankruptcy and insolvency matters and corporate restructurings. He is a member of the Insolvency Institute of Canada and of its board of directors, and is also a member of the American Bankruptcy Institute, the Turnaround Management Association, the Canadian Insolvency Association and INSOL.

He has been recognised by the following organisations as a leading expert in restructuring and insolvency: *Chambers Global*, *The International Who's Who Legal*, *Lexpert*, *Best Lawyers in Canada*, *PLC Cross-Border Restructuring and Insolvency Handbook*, and *PLC Which lawyer?*.

He has had significant involvement in the following public matters: *Abitibi Consolidated Inc* (pulp and paper), the restructuring of the Canadian Asset-Backed Commercial Paper (ABCP), *Quebecor World Inc* (printing), the liquidation of the Norbourg and Evolution Mutual Funds, *Cinegroupe Inc* (cinema), *Pangeo Pharma Inc.* (pharmaceutical), *Air Canada* (transportation), *Canada 3000* (transport), *Boutiques Jacob Inc* (retail), *Dumoulin* (retail) and *MAAX* (manufacturing). He also teaches the insolvency and bankruptcy course at the Law Faculty of the University of Ottawa.

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