Industry Canada Industrie Canada

National Insolvency Forum

Vancouver Regional Report

CAVEAT: The views expressed, suggestions made and/ or the discussions summarized in this Report do not necessarily reflect the opinions and/or views of the Office of the Superintendent of Bankruptcy.

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Foreword

As a result of the numerous revisions made to the *Bankruptcy and Insolvency Act (BIA)* over the past seven years, it was felt that 1999 would be an ideal time to consult with various stakeholders and practitioners regarding the operational aspects of Canada's Insolvency System. At an early stage in the process of organizing the National Insolvency Forum (NIF), we realized that, in order for these consultations to be successful in focussing on the operational aspects of the insolvency system, it was imperative that those participating possess a high degree of practical everyday *hands-on* experience. In other words, we wanted the NIF to be a Forum devoted to those practitioners and stakeholders who are the principal users of the system and who deal with the procedures and intricacies of the insolvency system on a daily basis. It is our opinion that the forum utilized has proved to be an ideal vehicle to accomplish our objectives and that the high degree of knowledge and expertise of participants has been an invaluable component to the success of these consultations.

Our Approach to the Challenge

In keeping with our mission of providing an effective, cost-efficient and uniform national program, as well as ensuring that the existing system is streamlined to better respond to stakeholders' needs, six (6) regions were selected to participate in the NIF initiative undertaken by the Office of the Superintendent of Bankruptcy (OSB).

The following Regional Report is one of six (6) reports which outlines the highlights of stakeholders' discussions and suggestions for changes and improvement to Canada's Insolvency System. A copy of the report will be forwarded to each participant and all reports will be published on the OSB web site (http://osb-bsf.ic.gc.ca). The National Report will be published in the upcoming *Insolvency Bulletin.*

In order to ascertain what works, what doesn't work, and what improvements can be made, stakeholders were asked to voice their concerns regarding the existing insolvency system.

In order to appropriately reflect the opinions and concerns expressed by the participants and stakeholders respectively, we have divided the Report in two (2) parts: *Part I* reflects the participants' discussions as to the efficiency of our existing system, including suggestions to streamline the process for consumer insolvencies, whereas *Part II* encompasses the participants' discussions on the same subject-matters, as they pertain to commercial insolvencies.

Finally, you will note that we have included in Appendix A a summary of various papers submitted by participants, as well as a list of the participants in Appendix B, for your perusal.

Part One
Consumer Insolvencies
Summary of Discussions & Key Points

1. Efficiency of the Current System

1.1. Streamlining the Existing System

With the millennium only a few months away and given the constantly changing nature of economic activity in Canada and throughout the world, it has now become imperative that Canada maintain a strong, vibrant and equitable insolvency system. The question then becomes *How efficient is our current insolvency system ?* To this end, both consumer and commercial representatives were invited to voice their views on a number of issues regarding ways to simplify the existing process and make it less time- consuming, more effective and cost-efficient.

The first issue on the subject of streamlining referred to **Counselling Services**. Participants encouraged the OSB to adopt a standardized national counselling module to ensure that debtors are actually obtaining worthwhile information. As a starting point, participants referred to the Money Management Program by Lawrence Westguys & Associates which could be used as an example of an established standardized model of financial counselling. The Canadian Bankers Association and VISA were also said to have developed similar programs that could be useful.

As well, it was suggested that the OSB consider studying the impact counselling has had on the number of repeat bankruptcies since its introduction, in order to ascertain its benefits. As a policy issue, some felt that the mandatory nature of counselling should be eliminated and left to the discretion of the trustee. Others believed that the practice of group counselling sessions was not as beneficial as they had intended and that it was important that counsellors and/or trustees spend time with bankrupts to deal with their particular situations on a one-to-one basis.

The OSB was encouraged to adopt a standardized national counselling module to ensure that debtors are actually obtaining worthwhile information and to study the impact counselling has had since its introduction in order to determine its benefits.

On the issue of **Student Loans**, it was suggested that the *BIA* be amended to provide that student loans may, under certain circumstances, be included in a consumer proposal in cases of financial hardship. To have rendered student loan undischargeable for ten (10) years following the end of a student's period of studies was seen by many as heavy-handed and unnecessary.

It was recommended that the BIA be amended to permit that student loans be included in a consumer proposal in cases of financial hardship.

Regarding **Proof of Claims** ("poc"), participants suggested that trustees should indicate in the initial bankruptcy documentation whether they anticipate distributing a dividend to creditors. They further mentioned that if a dividend was unlikely, they could then determine whether or not to file a "poc". It was said that such notification would avoid that creditors spend time preparing a "poc" where no dividend was probable.

It was suggested that trustees be required to send a Notification of Anticipated Dividend to all creditors in order that they may determine whether or not to file a proof of claim.

On the subject of the **Directive m12 on the Terms of Discharge**, participants identified problems of consistency in the application of paragraph 4b) which allows the trustee to recommend a conditional discharge in cases where the total amount paid to the estate by the bankrupt is disproportionate to the bankrupt's indebtedness and financial resources. Some trustees were said to be using this provision of the directive as a "catch all" to require additional payments, without justification, in all cases where the bankrupt has surplus income.

The OSB should provide clarification regarding the proper interpretation of paragraph 4b) of Directive m12 which allows the trustee to recommend a conditional discharge in cases where the total amount paid to the estate by the bankrupt is disproportionate to the bankrupt's indebtedness and financial resources.

Participants were generally in favour of the use of **Emerging Technologies** to streamline Canada's insolvency system. Participants favoured the use of electronic forms, e-filing, and tele-conferencing or video-conferencing for meetings of creditors and discharge hearings in addition to using electronic signature authentification software. As

well, it was suggested that the OSB consider the development of an e-mail system which could be used by the public to disclose any alleged wrongdoings by bankrupts. It was further proposed that the OSB use its web site to publish all notices of bankruptcy on a daily basis.

The OSB should examine the possibility of implementing various emerging technologies in order to further streamline the insolvency system.

1.2. The Realization of Assets & the Statement of Affairs

Many participants felt that more emphasis should be placed on the timely **Realization of Assets**, particularly when no lien or security exist against the assets. Creditor representatives felt this was an important issue when dealing with assets such as vehicles which tend to depreciate on a monthly basis or when such assets are stored, in order to reduce storage fees. Participants commented that it was a common occurrence to have much of the proceeds realized from the recovery of assets used to pay for the services of bailiffs or storage fees. Finally, it was mentioned that it would be beneficial if trustees would include more details as to the condition and location of the secured assets on the initial documentation sent to creditors.

Creditors mentioned the importance of a timely realization of assets in order to minimize depreciation of certain assets and/or reduce storage fees. They further commented that more detailed information and better communication regarding secured assets would be beneficial both to secured creditors and debtors.

Some participants commented that the insolvency community was doubtful as to the usefulness of the **Statement of Affairs** (SOA) and argued that even where a bankrupt does make false statements regarding his/her assets, or hides assets, there are seldom any sanctions imposed under section 198 of the *BIA*, as it is often difficult to establish fraud under the Criminal code's burden of proof.

As a general observation, there seemed to be an expectation gap between what creditors expect from a verification of the SOA and what the trustee actually does. Some participants commented that trustees were not probing enough and were not sufficiently inquisitive regarding the bankrupt's affairs.

Accordingly, it was proposed that the OSB develop a standardized list of questions for

debtors which would be attached to, and form part of, the SOA in order to assist creditors and trustees in identifying dishonest dealings and paint a more accurate picture of the bankrupt's affairs. Finally, there was some support for the creation of a creditor community education group that would consist of semi-annual day-long seminars bringing both the creditor and trustee communities together to deal with these issues collectively.

In order to better probe the bankrupt's affairs, it was proposed that the OSB develop a standardized list of questions for debtors which would be attached to, and form part of, the statement of affairs.

2. Service Standards

Participants recognized that the OSB was becoming more accessible to stakeholders and appreciated the consultations undertaken through the NIF initiative.

Moreover, a general comment was made suggesting that disciplinary hearings be disseminated in a wider fashion by publicizing their outcome in newspapers, in the *Insolvency Bulletin* and/or on the OSB web site.

On the issue of **Trustee Service Standards**, participants made three specific recommendations. Trustees should respond to correspondence within thirty days, return secured assets to creditors within thirty days, and promptly provide details to creditors regarding inquiries on the existence and location of assets in the bankrupt's possession.

Participants suggested that trustees respond to correspondence within thirty days, return secured assets to creditors within thirty days and promptly provide details to creditors regarding inquiries on the existence and location of assets in the bankrupt's possession.

Part Two
Commercial Insolvencies
Summary of Discussions & Key Points

1. Efficiency of the Current System

1.1. Streamlining the Existing System

The same questions were put to commercial and corporate participants regarding ways to improve the existing insolvency system and for making it more efficient and less time consuming.

The issue of **Commercial Proposals** was first raised as an area where improvements could be made to the insolvency process. The suggestion was that trustees take reasonable steps to ensure that a proposal be acceptable prior to it being submitted to creditors in order to reduce the number of cases where debtors resort to this option merely to frustrate creditors.

Practitioners expressed that although such a recommendation is well intended it is often difficult, if not impossible, to ascertain the *bona fide* proposal in cases where the debtor company approaches the trustee on the 8th, 9th or 10th day following receipt of a notice of intention from secured creditors to realize on their security under section 244 of the *BIA* or under provincial legislation. Participants commented that in those cases, the trustee is unable to distinguish between debtors acting in good faith and those who simply wish to delay and frustrate creditors as he/she does not have the appropriate financial records to make such a decision. In such scenarios, upon the filing of the notice of intention, the insolvent person is granted the stay of proceedings before the trustee can ascertain whether or not a viable proposal will subsequently be filed. Participants further added that the financial records of debtors experiencing financial difficulties are oftentimes in complete disarray which tends to further complicate matters.

> *It was proposed that, where possible, trustees take reasonable steps to ensure that a proposal be acceptable prior to it being submitted to creditors in order to reduce the number of cases where debtors resort to this option merely to frustrate creditors.*

Participants further proposed that **Cash Flow Statements** (CFS) be automatically forwarded to all creditors which is not currently the case. The CFS would help creditors evaluate more accurately the chances of success of the debtor's proposal.

As well, participants commented on the timeliness of the report sent before the meeting of creditors on the proposal. As a general observation, participants felt that, between the time the trustee's report is received and the date the meeting is held, they are not afforded sufficient time to make an informed decision on whether or not to accept the proposal. It was, therefore, suggested that this report be sent to creditors on the date the proposal is filed.

Participants suggested that cash flow statements be automatically provided to all creditors in order to assist them in their evaluation of the viability of the debtor's proposal. It was further suggested that the trustee's report be forwarded to creditors on the date the proposal is filed, thus allowing creditors more time to make an informed decision as to whether to vote for or against the proposal.

A debate then ensued on the appropriate degree of protection from liability offered to directors in a proposal. Some felt that this issue remains an aggravating problem as directors almost invariably resign all at once when a notice of intention is filed which greatly diminishes the potential of a successful reorganization given the sudden loss of qualified and knowledgeable individuals. Others cautioned that a careful balancing act must be maintained between the protection afforded to directors and their potential liability in reorganizations. It was argued that in most cases, without potential director liability there would be very little left for certain creditors (e.g., employees).

Participants noted that the *BIA* is silent on the issue of how **Meetings of Creditors** should be held. It was, therefore, proposed that alternative methods of physically attending a meeting be formally recognized in the *BIA*. It was said that such an approach would reduce the expenses incurred by creditors and increase their participation.

It was suggested that alternative methods of holding meetings of creditors be formally recognized in the BIA.

Stakeholders turned their attention to other **Miscellaneous Issues**.

Requirement to File an Assignment or Proposal in the Locality of the Debtor: One improvement that could be made to the *BIA* would be to permit a debtor to file proceedings in the locality of its counsel or trustee. Further flexibility could be added by providing that the filing can be done where the majority of creditors are situated.

Intellectual Property: Consideration be given to elaborate on the intellectual property rights under the *BIA*, such as the use of copyrights, licensing, etc.

Debtor in Possession Financing: The rules regarding DIP financing should be clearly established under the *BIA*.

2. Current Issues in Commercial Insolvencies

2.1. Unpaid Suppliers

Certain participants argued that section 81.1 and 81.2 of the *BIA* along with Purchase Money Security Interests under provincial legislation have had a negative impact on the credit made available to business. As a result, the risk of financing businesses has shifted to suppliers more than ever before. Consequently, the importance of having effective protections to safeguard suppliers from the additional lending risk has therefore become even more important.

As a way of addressing the lack of protection offered to **Unpaid Suppliers**, it was suggested to adopt a provision similar to *Personal Property Security Act* (PPSA) legislation in British Columbia which permits suppliers to benefit from a deemed security interest.

A further suggestion was made that a more effective time limit for reclaiming goods be adopted and calculated from the date of bankruptcy rather than from the date of delivery of said goods. With regard to the rights of unpaid suppliers in a proposal, it was recommended that suppliers benefit from some form of protection under a notice of intention or proposal and that their rights be re-affirmed in the event that the proposal is rejected by creditors or by the court.

It was recommended to amend the BIA to increase the protection for unpaid suppliers and provide them with a more effective time line to reclaim goods in a bankruptcy or a proposal.

2.2. Asset Rollovers

On this issue, one participant suggested that if the OSB is serious about eliminating **Asset Rollovers**, it should consider the recent British insolvency legislation amendments which provide that the owner, director or officer of a business, which has file for

bankrupt, be precluded from again holding such status for a period of 3 years, unless there

are extraordinary circumstances which could justify an exception to the rule.

Other participants argued that it often makes good business sense to entertain a proposal from the former owners and to allow assets rollovers to take place provided the best market value is obtained for the assets in question. As well, a comment was made that it would not be prudent to punish all owners, officers and directors as most bankruptcies are honest and non-abusive or fraudulent. Alternatively, it was proposed that such a restriction be imposed only in those cases, where it was established that former owners, officers or directors had committed abuses of fraud.

Most participants agreed that such transactions should be permitted provided the assets are rolled over at the best market value possible under the circumstances. However, some participants proposed that restrictions be imposed where cases of abuse and/or fraud can be established.

2.3. Receiverships

Although most participants acknowledged that Part XI of the *BIA* was introduced to ensure transparency and fairness in **Receiverships**, many felt that the requirements were onerous for small businesses receiverships. To address this problem, it was suggested to exclude smaller receiverships from complying with the requirements of Part XI, or alternatively provide a more cost-effective way of complying with said requirements. Other participants cautioned, however, that smaller receiverships still need to be administered openly and fairly and that it was imprudent to assume that smaller receiverships are less deserving of the protections of Part XI. Employees and creditors often just want to know which assets are being realized upon and the details of the disposition of these assets.

It was suggested to exclude smaller receiverships from complying with Part XI of the BIA or provide for a more cost effective way of complying with Part XI recognizing the need for a fair and transparent administration of all receiverships.

Part Three

The Time For *Action*

As you are aware, Phase I of the *Bankruptcy and Insolvency Reform* emerged in 1991 with *Bill C-22*. Phase II culminated in the enactment of *Bill C-5*, which was based largely on the Bankruptcy and Insolvency Advisory Committee (BIAC) recommendations in April 1997. Having now completed the National Insolvency Forum for the six (6) identified regions, the OSB must now draw from the numerous suggestions, a selected few which will be comprised in the Action Plan for the coming millennium.

The OSB will base its selection on various criteria such as the feasibility of the suggestion, the resources necessary to implement the suggestion, and whether the suggestion is in keeping with Government and/or OSB objectives and priorities.

Part Four

Executive Summary

Fiscal constraints and the pervasive question of *What taxpayers are getting in return for their investment in various government programs* have prompted the questioning and rethinking of traditional approaches to the role of government and how it does business.

While it is true that Integrity is the cornerstone of our insolvency system, it is also true that information on performance and efficiency is required for good management and effective governance. Knowing how well programs are doing is increasingly essential to managing today's public sector, as our government faces resource reductions and a citizenry that continues to expect good value from its government.

Although amendments made to the *BIA* during the 1992 and 1997 reforms have come along way in improving Canada's insolvency system, during the course of the NIF round table discussions, the OSB was made aware of a number of outstanding issues which warrant its attention in order to further improve the system. We have attempted to paraphrase those suggestions and recommendations made by both consumer and commercial insolvency representatives, in the following Executive Summary.

When asked *How to improve and streamline the process*, consumer insolvency stakeholders had a number of suggestions. The first issue on the subject of streamlining

deals with **Counselling Services.** Participants encouraged the OSB to adopt a standardized national counselling module to ensure that debtors are actually obtaining worthwhile information and to study the impact counselling has had since its introduction in order to determine its benefits.

On the issue of **Student Loans**, it was recommended that the *BIA* be amended to permit that student loans be included in a consumer proposal in cases of financial hardship.

Regarding **Proof of Claims**, it was suggested that trustees be required to send a Notification of Anticipated Dividend to all creditors in order that they may determine whether or not to file a proof of claim.

On the subject of the **Directive m12 on the Terms of Discharge**, participants suggested that the OSB provide clarification regarding the proper interpretation of paragraph 4b) which allows the trustee to recommend a conditional discharge in cases where the total amount paid to the estate by the bankrupt is disproportionate to the bankrupt's indebtedness and financial resources.

As another way of streamlining our insolvency system, participants were in favour of using **Emerging Technologies** and they proposed various emerging technologies be implemented by the OSB.

On the topic of **Realization of Assets**, creditors mentioned the importance of a timely realization of assets in order to minimize depreciation of certain assets and/or reduce storage fees. They further commented that more detailed information and better communication regarding secured assets would be beneficial both to secured creditors and debtors.

With respect to the **Statement of Affairs**, there seemed to be an expectation gap between what creditors expect from the statement of affairs and what the trustee actually does. As well, in order to better probe the bankrupt's affairs, it was proposed that the OSB develop a standardized list of questions for debtors which would be attached to, and form part of, the statement of affairs.

Finally, on the issue **Service Standards**, participants made three suggestions. They proposed that trustees respond to correspondence within thirty days, return secured assets to creditors within thirty days and promptly provide details to creditors regarding inquiries on the existence and location of assets in the bankrupt's possession.

When asked about the efficiency of our insolvency system, corporate and commercial participants were concerned, amongst other things, with the issue of **Commercial Proposals**. It was proposed that, where possible, trustees take reasonable steps to ensure that a proposal be acceptable prior to it being submitted to creditors in order to reduce the number of cases where debtors resorted to this option merely to frustrate creditors.

Regarding **Cash Flow Statements**, it was suggested that they automatically be provided to all creditors in order to assist them in their evaluation of the viability of the debtor's proposal. It was further suggested that the trustee's report be forwarded to creditors on the date the proposal is filed, thus allowing creditors more time to make an informed decision as to whether to vote for or against the proposal.

With respect to the issue of **Meetings of Creditors**, it was suggested that alternative methods of holding meetings of creditors be formally recognized in the *BIA*.

On the issue of **Unpaid Suppliers**, it was recommended to amend the *BIA* to increase the protection for unpaid suppliers and provide them with a more effective time line to reclaim goods in a bankruptcy or a proposal.

Insofar as **Asset Rollovers** were discussed, most participants agreed that such transactions should be permitted provided the assets are rolled over at the best market value possible under the circumstances. However, some participants proposed that restrictions be imposed where cases of abuse and/or fraud can be established.

Finally, the discussion closed by addressing the issue of **Receiverships** where it was suggested to exclude smaller receiverships from complying with Part XI of the *BIA* or provide for a more cost-effective way of complying with Part XI recognizing the need for a fair and transparent administration of all receiverships.

Part Five

Conclusion: The Way *Ahead*

The publication of this report marks an important step in the OSB's commitment to streamline and improve Canada's Insolvency System.

This series of NIF conferences has provided the OSB with insightful information on how to improve the existing Insolvency System. The OSB will now begin considering which suggestions can be implemented in the absence of legislative amendments through the issuance of *Circulars, Directives* and voluntary codes of conduct. With the next legislative review in 2002 just around the corner, proposals requiring legislative changes to the *Bankruptcy and Insolvency Act* will be formally submitted to the Corporate Law Policy Directorate of Industry Canada.

It is with your co-operation, through this type of round-table discussion, that the OSB, together with Industry Canada, will continue striving towards a business-like bankruptcy service which provides high-quality, trusted, timely and efficient services, consistent with its mandate.

We would like to reiterate our gratitude for your participation in the National Insolvency Forum (NIF). The Vancouver Conference was well attended and the suggestions for change and improvement to Canada's Insolvency System were very much appreciated.

Thank you, once again.

APPENDIX A

SUMMARY OF DISCUSSION PAPERS SUBMITTED BY PARTICIPANTS

DISCUSSION PAPER #1

Submitted By: The Canadian Bankers Association

CONSUMER BANKRUPTCIES & PROPOSALS

STREAMLINING (consumer proposal)

- Subsection 66.12 (2) of BIA should be amended to allow creditors to oppose a debtor moving from Division I to Division II. This will make it clear that debtors who have no intention of going through with a proposal cannot stop proceedings under one Division of the BIA and move to another Division, frustrating creditors in the process.

- Subsection 128 (1.1) of BIA should be amended to require due diligence on the part of the trustee in providing full names and addresses of any persons holding security interests. For example, if an incorrectly addressed notice is received by a large organization, it may well find itself outside of the thirty-day response period and lose its security.

- Section 66.2 of the BIA, regarding supervision of consumer debtors' affairs, should be amended to remove the requirement for obtaining the consent of the consumer.

TRUSTEE OFFICES

- A better consistency on the part of the trustee in addressing the spirit and intent of the legislation would improve the effectiveness of the BIA. The CBA recommends a consistent direction to trustees that they should immediately retrieve all collateral and credit cards and advise banks immediately of these measures.

- Some trustees take possession of collateral and often store it in private locations which incurs exorbitant storage costs for the financial sector. In addition, the delay in notifying the creditor of the fact of possession and location of the collateral exacerbates the problem.

DISCUSSION PAPER #2

Submitted By: Equifax

QUALITY, TIMELINESS AND COSTS OF INFORMATION RECEIVED BY THE OSB

- Only about one half of the information is received in a form which allows it to be added to the Equifax database in an automated fashion. The OSB should put procedures into place which ensure that information entered by department officials for circulation to both the general public and the credit reporting agencies is as accurate and complete as possible. In addition, it would be helpful if the OSB would provide information such as "trade style"

and “trade names” when an individual who has operated an unincorporated business is filing under the BIA.

- Bankruptcy related information must be delivered in a timely and accurate manner if it is to be a useful tool to credit grantors. This information must be made available on a real time basis. The OSB should consider converting their system to allow for such information to be sent on a daily basis via the Internet.

- Several months ago, the OSB imposed a very substantial user fee for obtaining bankruptcy related information. The OSB should opt to maintain the current rates it charges for information. These increased funds should be reinvested in a manner that will ensure enhancement of the product being delivered.

ON-LINE CREDITOR AND DEBTOR LISTS

- This information should be made public immediately upon same being compiled by the appointed receiver or trustee. Such information should be made available by means of a universally accessible web site at no charge to the general public. The current system tends to favour one class of creditor over others. The OSB initiative should strive to ensure greater equity in the dissemination of information, a concept which certainly would be appropriate and fair.

DISCUSSION PAPER # 3
Submitted By: The Canadian Bankers Association

COMMERCIAL BANKRUPTCIES & PROPOSALS

I) STREAMLINING

- There should be common service delivery standards for Insolvency Professionals. Banks find a wide variety in the quality and timeliness of reports received from IPs which makes it difficult for banks to respond and participate effectively in the process.

- Brief interim reports should be made available to all creditors indicating progress made in finalizing the bankruptcy.

- An updated asset and liability report should be provided after claims have been proven and assets have been formally appraised or investigated.

- Attendance at a meeting of creditors should not be necessary, except in cases of fraud, missing assets, etc.

- Time frames for voting on a proposal seem too short as it appears the documents are not always mailed promptly.

II) RECEIVERSHIPS

- Registration and compliance with the receivership provisions of the BIA are onerous for some businesses. In many instances, the cost of appointing a receiver to meet BIA requirements exceeds the realizable value of the assets held as security.

III) ENVIRONMENTAL LIABILITY

- The CBA opposes any "super-priority" liens which change the priority scheme that is relied upon by secured creditors.
- The scope of any super-priority for environmental clean-up costs must be strictly limited
- Limiting the super-priority on a site-by-site basis to the "affected property" only, is the best solution.
- The words "is contiguous thereto" [subsection 14.06(7)] should be replaced by "has a common boundary therewith".

IV) INTERNATIONAL INSOLVENCIES

Any BIA international insolvency amendments should not:

- interfere with the discretion of Canadian judges;
- impact on the flexibility of courts to deal with debtors and assets located in Canada;
- facilitate the importation of foreign bankruptcy laws;
- introduce uncertainty into domestic lending transactions or the taking of security;
- constitute leading edge cross-border insolvency legislation.

V) DEBTOR IN POSSESSION FINANCING

- The courts are now exercising inherent jurisdiction to grant super-priority charges over existing lenders to secure financing for businesses that are now under reorganization. It will be important for the banks as lenders that the criteria for such super-priority financing be better defined in restructuring legislation.

VI) DIRECTORS' OBLIGATIONS

Directors should:

- be given a degree of protection in insolvency situations from strict liability for claims such as wages and source deductions which can arise without the fault of the directors;
- have a fiduciary duty to consider the interests of creditors as well as shareholders.

VII) LEASING

- Clearer and more consistent rules governing leases of personal property should be developed. For example, there is considerable uncertainty as to what happens when a lessor goes bankrupt. It is unclear to what extent lessors are secured creditors for the purposes of the BIA and the CCAA. There is no process for retaining or disclaiming personal property leases. Addressing these issues should simplify leasing financing.

VIII) PRIORITIES

- The new super-priority for source deductions should be limited to current assets.
- The bankruptcy scheme of claims priorities should apply in receiverships.

IX) INTELLECTUAL PROPERTY

- Reform in the area of intellectual property rights would enhance both the lending process and the insolvency process, given the growing importance of intellectual property rights in many businesses.

X) UNPAID SUPPLIER

- Complete removal of the “unpaid suppliers” provision from the BIA (sec. 81.1): this provision has a negative impact on the availability of credit as it reduces the ability of borrowers to pledge inventory as security for advances of credit, thereby curtailing access to inventory and operating financing.

DISCUSSION PAPER #4
Submitted By: The Corporate Law Policy Directorate, Industry Canada

This paper outlined the consultation and policy development process that Industry Canada intends to pursue during the next phase of reform to the BIA and CCAA, and will discuss some of the key issues that will need to be addressed in the latest phase.

THE PROCESS

In the first phase of bankruptcy reform, a two-stage process was followed. In the first stage, an Advisory Committee on Bankruptcy and Insolvency was created by the Minister of Consumer and Corporate Affairs. The Committee was tasked with examining the bankruptcy and insolvency system, assessing possible reforms and recommending amendments to the *Bankruptcy and Insolvency Act*. This was followed by a second stage, of largely bilateral consultations and negotiations between the Department of Consumer and Corporate Affairs and insolvency stakeholders. The result was Bill C-22, which finally emerged in 1991. The bilateral consultation process employed in the second stage of Phase 1 proved cumbersome and inefficient.

In Phase 2, Industry Canada sought to overcome this by carrying out its consultation through a Bankruptcy and Insolvency Advisory Committee (BIAC) in which all key insolvency stakeholder groups were represented. BIAC was tasked with providing for the exchange of advice and information, identifying insolvency issues and proposing solutions and providing feedback on government policy and legislative proposals, in

addition to building a consensus to facilitate change. Phase 2 culminated in the enactment of Bill C-5, which was based largely on the BIAC recommendations, in April 1997.

Our challenge in Phase 3 is to establish a consultation and policy development process that retains the many benefits of the BIAC process while addressing some of the issues left unresolved. Industry Canada is planning a two-stage policy development/ consultation process. In the first, pre-consultation stage, the Department will produce a series of discussion papers for distribution to insolvency stakeholders in 1999-2000. These papers will set out the issues which we believe must be addressed to ensure that our current insolvency laws provide a modern, efficient and effective legal framework. During the second stage, stakeholders will be invited to submit their comments, their own priority issues and position papers. Policy review sessions will then be held in various localities across Canada as warranted by the subject matter. The policy review sessions will be a key element of the consultation process.

Sessions will focus on getting stakeholder concerns and views as to how issues should be addressed. We expect the first round of policy review sessions to be completed early next year. The Department will then revise its discussion papers and arrange a second set of review sessions later in 2000. This process may be repeated for additional issues and policies through to the end of 2001, at which time a final report will be drafted. This process will allow for effective participation by non-experts and regional stakeholders. Furthermore, it will force the development of feasible preliminary options with respect to contentious issues and an initial overall review of the major elements of insolvency law in Canada.

SOME KEY ISSUES

A) CONSUMER ISSUES

1. Exemptions for RRSPs and personal property

Both issues will be discussed: whether to exempt RRSPs in bankruptcy, and whether to replace the current personal exemption provisions, that adopt provincial rules, with a federal code.

2. Availability of credit, and debtor and creditor responsibility for high consumer debt

The issues are whether, and if so how, to discourage easy credit for high risk consumer debtors and whether, through legislation, to impose responsibility on consumer debtors or lenders or both.

3. Student loans

The 1997 and 1998 amendments to the BIA enacted a non-dischargeability period for student loan debts. However, student representatives have been critical of it and the

Canadian Federation of Students has announced its intention to challenge the extension under the Charter of Rights.

B) COMMERCIAL ISSUES

4. Stays of Proceedings in Commercial Reorganizations

The BIA provides that the court may lift a stay imposed on a creditor in a BIA proceeding if it is satisfied that the creditor will be materially prejudiced. The issue is whether to establish more precise rules regulating the availability of stays in Canada.

5. Contractual Rights in Reorganizations and Bankruptcies

In Phase 3 we need to examine whether to further modify existing rules or to establish specific rules governing termination or adoption or enforcement of other types of contracts, including technology contracts, collective agreements and supply contracts.

6. Debtor Financing During Reorganizations

Obtaining financing is a critical concern of debtors seeking to reorganize under the BIA or CCAA. An issue for Phase 3 is whether to provide stronger protection to providers of credit to insolvent debtors during BIA or CCAA reorganizations in order to enhance the availability of credit.

7. Consolidation of the BIA reorganizations scheme and the CCAA

The question has been raised as to the need for a separate statute to deal with reorganizations of large corporations. The question is whether to bring the CCAA into Part III of the BIA.

8. Director/officer responsibilities

Directors are exposed to liability for specific types of claims, such as tax and wage claims, under a variety of federal and provincial statutes. Most directors' liability legislation gives directors due diligence defences against liability. One issue is whether to provide stronger protection to directors in insolvency cases to encourage directors to continue guiding a company through a restructuring. Another issue is whether to provide additional constraints on directors whose conduct is below a certain standard. One such constraints could be to restrict the ability of principals of a bankrupt company to acquire its assets and set up a business again. Another could be to provide for disqualification of directors and officers who are responsible for bankruptcies.

9. Vantage Securities

The task now is to determine the facts of this complex case to see if they raise issues whose resolution requires amendments to the BIA.

C) PRIORITIES

10. Crown priorities - Workers Compensation Board (WCB) claims and tax claims

Difficult Crown priority issues remain outstanding for Phase 3: federal and provincial treasuries want stronger protection for GST and sales tax claims. Some provinces want better protection for property tax claims and WCB claims. On the other hand, the private sector remains opposed to any expansion of Crown priorities and has expressed some concern about recent legislation intended to strengthen existing priorities.

11. **Wage claims**

The question remains as to whether and, if so how, to provide better protection to wage earners in their employers' bankruptcy and who should bear the cost - other creditors through a super priority provision or taxpayers (and if so, which taxpayers - employers, employees or taxpayers generally?) through a fund.

12. **Unpaid supplier claims**

The provisions concerning unpaid suppliers have been criticized as providing limited and uncertain protection - they apply to goods only, not services and only if the goods have not been altered or resold since delivery. The issue is whether to improve the status of supplier claims in bankruptcies and reorganizations.

13. **Consumer liens**

We need to consider whether there is a need to improve the status of claims of consumers for goods paid for but not delivered by insolvent businesses.

14. **Wage assignments**

When the Phase 2 amendments were before Parliament, the credit unions, who rely on wage assignments as security, sought to have the 1992 amendments repealed and wage assignments again made enforceable in bankruptcy. They also stated that wage assignments were one of the few types of security which many of their customers could give and that restrictions on it reduced the credit available to those customers. The issue in Phase 3 is whether to reinstate the enforceability of wage assignments in bankruptcies.

D) OTHER ISSUES

15. **Adopting the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvencies**

UNCITRAL developed a Model Law on Cross-Border Insolvencies, which was adopted by the U.N. General Assembly in late 1997. Canada was an active participant in the UNCITRAL discussions. During Phase 3, we need to consider whether we should adopt the UNCITRAL Model Law on Cross-Border Insolvencies.

16. **Consolidation of legislation governing insolvencies of financial institutions**

The *Winding-Up and Restructuring Act* has been substantially amended to make it an adequate vehicle for financial institution liquidation. Given that Finance has the lead on

whether to further modernize the WURA, what Industry Canada needs to consider is whether to restrict the application of the Winding-Up and Restructuring Act to financial institutions.

17. **Trustee Liability**

The 1997 amendments, including provisions protecting a trustee who carries on the business of a debtor or continues employment of the debtor's employees from liability for claims arising before his appointment, have been criticized as being ineffective to protect a trustee. In this round of reform, we need to examine whether to address the issues raised by St. Marys Paper by providing further protection to trustees and receivers.

18. **Preferences and Settlements**

The issue for Phase 3 is whether to consolidate and modernize Sections 91 to 101 of the BIA in the way the 1975-84 omnibus bills would have made more far reaching changes to those provisions.

DISCUSSION PAPER #5

Submitted By: Western Forum of Credit and Financial Executives Association

HOW DO WE STREAMLINE AND RENDER THE EXISTING SYSTEM LESS TIME-CONSUMING AND MORE EFFECTIVE ?

- The OSB should introduce electronic data transfer of information that will:

  (a) speed up the notification to creditors, by a Receiver-Manager or Trustee, of actions under the BIA;
  (b) Allow for the electronic transmission of forms that could include Statements of Claims, scan documents and remove the requirement for notarized signatures to support same. This would require an electronic certification process to ensure that the party transmitting the data was authenticated.

- Repeal the CCAA and only augment those sections of the CCAA that will help support commercial proposals that have a reasonable chance of succeeding. The benchmark for accepting the proposal should be the opinion of the creditors as to whether the debtor company's proposal is reasonable.

UNPAID SUPPLIERS

- Improve subsection 81(1) of the BIA, regarding the return to suppliers of 30-day goods. Amendments should clearly indicate that removing an item from its skid, shrink wrapping, or other delivery packaging, and removing goods from their packaging material does not change the state of the goods delivered. Debtors should not be allowed to evade 30-day reclamation rights by deliberately changing the state of a product, e.g. putting a line of blue paint across plumbing supplies to change the state of the product. This fraudulent activity has been reportedly used to remove a supplier's 30-day return of goods.

- The protection offered to suppliers should be expanded to include obtaining goods sold to the debtor but held by 3rd party warehousemen, or others. Furthermore, any goods obtained through fraudulent activity, should be returned to the supplier of said products and not be used to reduce the debt of all creditors, or a specific creditor.

Investigations and enforcement of the BIA

- Parliament should adopt similar amendments to that of British bankruptcy law, which provides that where the owner of a business goes bankrupt, he/she cannot hold the position of a majority owner, director or shareholder for 3 years, unless there are extraordinary reasons which would justify an exception.

- Stiffer sentences for fraud are needed in terms of fines and incarceration, or other civil penalties. There is a lack of deterrence with current white collar sentencing. Obtaining goods through the commission of fraud or related offences should be offset by the seizure of assets.

- The current threshold for proving a fraud is so high as to make it nearly impossible to obtain convictions. The rewriting of legislation for both the Criminal Code and the BIA is absolutely essential to address this problem.

- Investigation teams should not be solely limited to police personnel, but be augmented with civilian expertise including, but not limited to, accountants, bankers and professional credit managers.

- Law enforcement and the OSB should maintain active liaison with various credit industry groups, in addition to working with credit reporting/collection agencies. This would enhance public education of the law, warning signs of fraud or BIA violations, and give law enforcement personnel good resources for information.

- Increase the investigative authority for inspectors appointed under the BIA to permit them more input and control of the bankruptcy proceedings. The increased authority should allow inspectors access to files of the Superintendent of Bankruptcy and police concerning questionable actions of a debtor or those aiding or abetting the questionable activities of the debtor.

- There are not sufficient police officers, or other investigators, and crown counsel to investigate and successfully prosecute white collar crime. The knowledge of BIA and Criminal Code fraud legislation by police personnel and many prosecutors is poor. In

  many instances the police will try to "pawn off" as "civil violations" actions which fall within the criminal realm. This is due to lack of knowledge and/or lack of support and resources.

- There is a lack of adequate funding for the RCMP, provincial and municipal police agencies and the OSB, to properly train and allocate manpower for commercial crime investigations.

C Funding of investigations and prosecution of white collar crime should come from seizures of assets gained through the commission of fraud. The proceeds should not be placed in the federal government's general revenue, but go directly into accounts established for future fraud investigations, necessary equipment, and related staffing of the police, crown counsel, courts, etc. The Government of Canada has an obligation to ensure the public is not victimized.

DISCUSSION PAPER #6

Submitted By: John R. Sandrelli, Heenan Blaikie, Barristers & Solicitors

- **DISCUSSION ON "LOCALITY OF THE DEBTOR"**

  Both Subsection 43(5) and Section 50.4 require that either the Petition for a Receiving Order or the Notice of Intention be filed within the "locality of the debtor". Further, although not specifically prescribed, it is assumed that a Proposal must be filed with the Official Receiver in the locality of the debtor. In certain circumstances, however, the debtor may have an interest in filing in a location other than his/her "locality" for reasons relating to the legal counsel chosen or an insolvency administrator.

- **WHAT WORKS ?**

  In cases of the filing of Petitions for a Receiving Order and in cases of voluntary assignments in bankruptcy, requiring filings in the locality of the debtor works well.

- **WHAT DOES NOT WORK ?**

  In the context of voluntary re-organizational proceedings under Part III of the BIA, debtors should have the opportunity to elect counsel of their choice as well as a Trustee of their choice without being constrained by location. Usually, in the context of voluntary Proposals under Part III, resources are limited and thus a debtor may be forced to give up his/her choice of elected counsel or insolvency administrator given the additional costs associated with travel and the like.

- **WHAT IMPROVEMENT CAN BE MADE ?**

  One improvement that could be made to the current legislation would be to permit a debtor filing a Notice of Intention or a Proposal under Part III to do so in his/her own locality as presently defined under Section 2 of the BIA or in the locality where his/her chosen counsel or Trustee practice or has its main office. This improvement could be accomplished by amending the definition of "locality of the debtor" in Section 2 of the BIA to include in a new subparagraph (d) "where the debtor's counsel or the Trustee appointed under the Proposal or Notice of Intention has its head office".

- **DISCUSSION ON TAXATION ISSUES**

  In more complex bankruptcies or reorganizations, issues of taxation can be quite complicated and time-consuming, especially in the event of the taxation being conducted by a Registrar or a Judge who is not familiar with the main proceedings. In such circumstances, it is obviously efficient to hold the taxation before the Judge involved in the

main proceedings. It may be appropriate for the Rules to be amended to provide that Bills of Costs for legal services may also be taxed by a Judge having jurisdiction in bankruptcy matters, at the direction of such Judge.

- UNPAID SUPPLIERS

  Under Sections 81.1 and 81.2, the rights of unpaid suppliers are not triggered unless the purchaser is bankrupt or there is a Receiver within the meaning of subsection 243(2) in relation to the purchaser. *In the Matter of Everfresh Beverages Inc.* and *In The Matter of J.S. McMillan Fisheries Ltd.*, Interim Receivers appointed under Section 47 have been held not to be "Receivers" for the purposes of Sections 81.1 and 81.2. As a result, the rights of unpaid suppliers and others are subject to abuse or manipulation in circumstances where an Interim Receiver could be appointed as opposed to a Receiver within that meaning of Section 243(2). Thus, one questions whether those rights should also arise in the event of the appointment of an Interim Receiver.

DISCUSSION PAPER #7

Submitted By: Joseph J.Leahy, Assistant Manager, Account Services, TD Bank Financial Group

I) DOCUMENTATION

Since 1990 there has been a steady upward trend in insolvency volumes, marked by irregular increases at times of regional economic recessions.

- As we prepare for the year 2000, and in view of a multitude of electronic commerce solutions now readily available to any business or government agency, the recommendation is that Internet-based services which allow trustees, creditors, the courts and other stakeholders to process standardized insolvency documentation, payments and remittances electronically and inexpensively should be considered.

II) CREDITOR AND TRUSTEE INTERACTION

A good portion of the financial and business services are efficiently managing their business within regional call and service centres. It is not uncommon for these centres to process several hundred proposals and insolvencies during any given month from a vast market place (geographically speaking).

- The OSB should give creditors the option of attending and voting upon matters at meetings of creditors by teleconference, regardless of geographic location.

- A flexible counselling program of the insolvency process could provide a uniform and measurable level of consistency of information to those impacted by insolvency and encourage feedback from trustees and all stakeholders.
- The counselling segment may consider inviting other areas of the financial community into the counselling and education roles to afford the ability to be responsive to the expectations of all stakeholders in the insolvency community.

DISCUSSION PAPER #8
Submitted By: Registrar Elizabeth Dunn, Supreme Court of British Columbia

- REHABILITATION OF THE BANKRUPT AS A VIABLE CONSUMER

  Even with the assistance of the trustee through the counselling process and the production of expense statements, the introduction of the bankrupt to the concept of budgeting has come too late. There should be two columns added to the existing schedule: one showing the percentage of the bankrupt's budget being spent on particular items and the second showing the recommended percentage. In discussion with trustees there have been suggestions that such matters as budgeting should be taught to high school students as part of a career and personal planning program.

- SECOND-TIME BANKRUPTS

  The goal of providing rehabilitation to the bankrupt is not being met. Given the increasing number of individuals seeking a discharge following their second bankruptcy, the duties of the bankrupt in the course of bankruptcy and the requirements for obtaining a discharge set out in the BIA, should be different for a repeat bankrupt. It is also suggested that there be a routine disclosure provision in credit applications regarding the existence of a previous bankruptcy. Prior to discharge, repeat bankrupts might be required to attend a night school course in financial management.

- THE ROLE OF CREDITORS

  Creditors who arrive at court to object to the discharge of a debtor are often surprised by the process and disappointed that they will not benefit directly from any conditional order made. The trustee should provide a detailed explanation of the role of the creditor in the bankruptcy process, particularly with respect to the discharge procedure.

- PROCEDURE
  There are six locations throughout the Province where bankruptcy matters can be heard. Several sections of the BIA determine where proceedings have to be filed. Given the significant costs and inconvenience to debtors, creditors and trustees, for traveling to relatively limited locations where bankruptcies are currently filed, it is suggested that the number of bankruptcy registries in the province be increased. While an increase in the number of registries accepting filings and hearing bankruptcy matters would require additional training, the cost of such training might very well be outweighed by the benefit to the bankrupt, creditors and trustees.

APPENDIX B

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