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National Insolvency Forum

Saskatoon 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.

Contents

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 and more effective and cost-efficient.

The discussion opened with the issue of **Discharge Hearings**. Pursuant to subsection 169.(2) of the *BIA*, the trustee is required to file an application for discharge of the bankrupt not earlier than three months and not later than one year following the bankrupt's assignment. Participants viewed this timeframe as too broad and suggested that the provision be amended in order to restrict its scope, alternatively it was proposed that such an application be presented only when the bankrupt had fulfilled all the statutory duties and obligations of the *BIA*.

A few participants noted that, in Saskatchewan, it is not uncommon to encounter a three month delay for a discharge hearing date. It was reported that, when a date is scheduled, oftentimes, parties are not ready to proceed. Moreover, participants stated that further delays are often incurred due to fact that creditors are allowed to file their objection on the day of the hearing and can simultaneously request an examination of the debtor which obliges the presiding registrar or judge to grant further an adjournment of the proceedings. It was, therefore, suggested that such practice be disallowed.

Moreover, participants were unanimous in recommending that discharge hearings be held via conference call and/or video-conferencing. It was mentioned that such an approach would save both time and money for all parties involved. It was further suggested that the *BIA* be amended to introduce a "*Notice of Intention to Object to a Bankrupt's Discharge*". It was suggested that creditors who intend to oppose the bankrupt's discharge be required to complete such a form prior to a specified date, in order to advise interested parties of their intentions. Participants added that this notice would

undoubtedly trigger an informal alternative dispute resolution mechanism between the trustee and the objecting party. Other participants held an opposing view arguing that an informal dispute mechanism would merely add another layer to the bankruptcy process thereby causing further delays. As an alternative, they suggested that the OSB and trustees concentrate their efforts on informing creditors of their rights and responsibilities regarding the discharge process.

It was suggested that the BIA be amended to introduce a Notice of Intention to Object to a Bankrupt's Discharge. It was further proposed that discharge hearings be held via conference call and/or video-conferencing rather than physical attendance. rather than physical attendance.

Participants discussed the **Stay of Proceedings**, and commented that whether this procedure is the result of an insolvent person filing a notice of intention or a proposal, or whether it is triggered by a person filing for bankruptcy, it is always intended to preclude a creditor from seeking recourse from a debtor and is oftentimes frustrating for creditors. Accordingly, it was suggested that the *BIA* be amended to provide that the stay of proceedings be limited to a period of 9 months, with the option of requesting an extension, if needed. In all other cases, the stay of proceedings would automatically be lifted at the end of the nine month period.

It was proposed that the BIA be amended in order to limit the stay of proceedings to a nine month period with the option of requesting an extension, if needed.

The discussion then proceeded to issues regarding the necessity of filing a **Proof of Claim** *(* "poc"). A large number of participants agreed, as another way to streamline the process, that creditors be required to file a "poc" only in those cases where it was likely that a dividend would be distributed to creditors. Alternatively, it was suggested that the Statement of Affairs (SOA) be used as *prima facie* evidence of the bankrupt's indebtedness to a creditor and that a "poc" be required, only in those cases where the creditor disagrees with the amount stated in the SOA, or where the trustee suspects questionable transactions or practices.

Participants mentioned that the issue of **Student Loans** should have been included in the NIF agenda. The large majority of those present felt that the amendment made to section

178 of the *BIA*, increasing the period for which a student loan may not be discharged from two (2) years to ten (10) years was inequitable and unjust. Many participants felt that the default rate on student loans was not out of proportion to other forms of loans or credit extension. According to many present, the solution to this problem, whether real or perceived, should have been either to include a hardship clause or alternatively, resort to mediation in order to settle the terms of re-payment or of loan forgiveness.

One participant even stated that the "ten-year rule" has promoted the incidence of bankruptcy amongst former students by encouraging them to use other methods of payment such as credit cards, personal loans, lines of credit, etc., to pay off the student loan portion of their debt load, then proceeding to declare bankruptcy once it had been eliminated.

Participants expressed dissatisfaction regarding the amendment to section 178 of the BIA and suggested that the provision be amended to introduce a hardship clause or alternatively provide for mediation in order to resolve the matter.

The discussion then turned to **Consumer Proposals** (Division II). Subsection 66.19(2)[1] of the *BIA* currently provides that related persons (i.e. spouses) may only vote against a proposal. Some participants, however, felt that this provision was inappropriate and suggested that it be amended to preclude related parties from voting for or against a proposal. The rationale given being that spouses not be permitted to pursue matrimonial conflicts in the insolvency arena. A second recommendation was made with respect to consumer proposals to the effect that the insolvent person be required to deliver all credit cards to the trustee upon the filing of the proposal, as is the case for a debtor who files for bankruptcy.

Participants suggested that the BIA be amended to prohibit related persons from voting for or against a consumer proposal. It was also proposed that the insolvent person be required to deliver all credit cards to the trustee upon the filing of the proposal.

Many participants believed that the current limit of seventy-five thousand dollars applicable to consumer proposals should be raised to two-hundred and fifty thousand dollars. It was also suggested that the consumer proposal regime be applicable to sole proprietorships. However, if such a recommendation were to be adopted, participants

[1] *Subsection 54(3) of the BIA provides essentially the same rule for commercial proposals (Division I).*

cautioned that consumer proposals would also have to provide for a stay of proceedings against secured creditors in order for this amendment to be effective.

It was suggested to amend the existing threshold of consumer proposals from seventy-five thousand dollars to two-hundred and fifty thousand dollars and that the consumer proposal regime be applicable to sole proprietorships.

On the issue of **Education**, many believed that the typical high school curriculum should provide a student with a sound foundation regarding budgeting principles and the responsible use of credit. To this end, it was proposed that the OSB lead the way to develop and implement a national program which would prepare adolescents to deal responsibly with the use of credit and the management of household finances.

Participants agreed that the OSB should play a prevalent role in developing and implementing a national program geared at educating our youth on the concepts of budgeting, credit and financial management.

As another way of streamlining the process leading to the issuance of a **Receiving Order**, some participants suggested that Canada follow in the footsteps of the UK and repeal all acts of bankruptcy except for that of paragraph 42.(1)(j) which provides that "*a debtor commits an act of bankruptcy if he ceases to meet his liabilities generally as they become due*". It was stated that the other motives for petitioning a debtor into bankruptcy are rarely, if ever, invoked and therefore serve very little purpose. At the very least, it was felt that this suggestion should be the object of further study.

It was suggested to amend the BIA to repeal all acts of bankruptcy, except paragraph 42.(1)(j) which provides that "a debtor commits an act of bankruptcy if he ceases to meet his liabilities generally as they become due".

1.2. The Realization of Assets & the Statement of Affairs

The discussion on this issue opened with participants suggesting that trustees be required, as a matter of course, to request a copy of the bankrupt's household insurance policy, particularly the section which deals with household contents. It was said that

oftentimes these policies comprise a list of all assets owned by the insured. This was considered to be an ideal way of verifying the accuracy of the **Statement of Affairs** (SOA) by way of comparing the assets listed in the policy with those declared by the bankrupt in the SOA.

It was further proposed that the *BIA* be amended in order to permit a trustee to file an amended SOA which would in turn be forwarded to creditors in those cases where additional and/or materially significant information was obtained regarding the debtor's assets. This suggestion was considered by some to be an excellent way of keeping creditors involved in the process.

One participant went so far as to suggest that the *BIA* be amended to preclude the debtor from an automatic discharge, after a nine-month period, in cases where the SOA was later found to be materially or significantly inaccurate.

The discussion then proceeded to a debate on whether trustees were asking debtors sufficiently probing questions regarding the existence of, or ownership in, certain assets. This led to the recommendation that a "National Assets Checklist" be developed and form part of the SOA, similar to that which is used in many provinces for "Matrimonial Property Checklist".

It was suggested that the BIA be amended to require the trustee to file an amended statement of affairs, which in turn would be forwarded to creditors in cases where additional information and/or materially significant information was obtained regarding the debtor's assets.

2. Service Standards

A brief discussion ensued on the issue of **Service Standards**. It was proposed that trustees be required to return phone calls within a day or so. It was further recommended that joint efforts between the private sector, the OSB and provincial government be made in order to establish a National Registry for personal property and credit searches. In addition, creditor groups also expressed the desire to be better informed as to their rights and responsibilities in a bankruptcy. Creditors added that it would be useful if this information was sent out with the notice of bankruptcy. This would allow them to make informed decisions throughout the bankruptcy process.

It was proposed that trustees be required to return phone calls within a specified timeframe (e.g., a day or so).

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 about ways to improve the existing insolvency system and make it more efficient and less time-consuming.

When asked about the efficiency of our insolvency system, corporate and commercial participants were concerned with the **Taxation of Accounts**. As a way to streamline the process, it was proposed that taxation be dispensed within three distinct situations, provided that the OSB and inspectors have been sufficiently informed, and that no interested party has objected: (1) for all legal services accounts; (2) for all estates where there are no assets and no contentious issues; and (3) in all estates where the trustee's fees do not exceed $5,000.

It was suggested that consideration be given to eliminate,in some cases, the current practice of taxing both legal and trustee accounts.

Meetings of Creditors were raised as an area where improvements could be made. The first recommendation was that meetings should be held only in cases where a certain percentage of creditors requested them. Although no specific threshold was suggested, many welcomed the suggestion and considered that it would be both an effective and efficient way of doing business. Others, however, cautioned that meetings of creditors can be very beneficial in that they offered creditors the opportunity to voice their

concerns as well as exchange information, which can sometimes lead to identifying questionable transactions and/or hidden assets.

The second recommendation regarding this issue was to permit that alternative means of physically attending meetings such as tele-conferencing and/or video-conferencing be recognized as viable options. Participants commented that the *BIA* should be amended to clearly provide for such means as a way of holding meetings.

It was suggested that meetings of creditors not be mandatory in all cases. However, in those cases where such meetings were necessary, it was suggested that the BIA be amended to clearly provide for alternative means of physically attending meetings.

The **Proof of Claim** ("poc") was then discussed. The initial comment of participants suggested that the "poc" form had become archaic in terms of wording and format and should be abolished or alternatively revised and simplified. Some of those present, were of the opinion that its use should be limited to those cases where the creditor contests the amount stated in the SOA. Others, considered the "poc" to be a very important and useful document for trustees to identify questionable transactions and proposed it be kept. However, they suggested that it be filed at a later time during the process in order that trustees be afforded more time to provide creditors with more complete information as to the debtor's assets. It was said that this approach would permit creditors to make a more informed decision as to whether or not to file a "poc".

Participants suggested that the proof of claim form be revised and simplified and that consideration be given to exempt creditors from filing a proof of claim, in certain circumstances.

The discussion on the efficiency of the current system ended with stakeholders turning their attention to a variety of other **Miscellaneous Issues**.

Former rule 89 of the *BIA:* This rule provided for a summary manner to proceed with section 91 to 100 applications. All practitioners agreed that *Rule 89* was very cost-effective and much less time-consuming than the normal channels of court procedure for adjudicating such disputes and that consideration be given to reinstate it.

Intellectual property*:* Given the growing importance and diverse range of intellectual property rights, a clearer definition of "intellectual property" would be beneficial.

Directors' Liability*:* Some participants felt that it is still quite difficult to retain or attract directors during a proposal and that more protection should be afforded to directors.

Estate Information Web Site*:* It was proposed that a web site be created for the exclusive use of posting information for the benefit of creditors and the general public regarding the status and details of bankruptcies.

2. Current Issues in Commercial Insolvencies

2.1. Unpaid Suppliers

Many participants felt that section 81.1 has caused more problems than it has solved. Its application is uncertain, at best, and provides no protection to **Unpaid Suppliers** in a receivership or a wind-up. Others felt that we should reapeal section 81.1 and begin anew. Two major problems were identified with the application of this section. The impractical time frame for reclaiming possession of goods and the issue of product identification. It was purported that for such things as feed, grain and fuel, it is virtually impossible for suppliers to benefit from the protection of section 81.1 as it is rarely possible to identify such supplies unless they have been clearly and specifically segregated.

It was further proposed that the term "same state"found in section 81.1 of the *BIA* be defined in order to afford unpaid suppliers appropriate protection. One participant added that this suggestion had even more weight in light of the recent case law which interpreted this term in a restrictive manner.

Representatives from financial institutions commented that the provision dealing with unpaid suppliers has had the effect of restricting the availability of credit. It was reported that banks and other credit grantors are now hesitant, or simply refuse to lend money in cases where the loan security consists of goods or supplies in inventory. Other participants refuted this explanation by stating that there was no evidence of this practice in the banking community.

A few participants justified the lack of protection made available to unpaid suppliers by commenting that too much protection was being granted to secured creditors. It was explained that secured creditors have the ability to realize on their security, upon the debtor's default of meeting his/her obligations, by virtue of the security agreement. Consequently, it was said that debtors will often go to great length to try and prevent this from taking place: the result being that debtors, while in the throes of insolvency, will tend to order large supplies of inventory which can easily be sold or liquidated with the proceeds channelled to secured creditors. It was, therefore, proposed that secured creditors be precluded from obtaining security on any goods delivered 90-days prior to the date of bankruptcy.

Moreover, it was proposed that the protection afforded to unpaid suppliers be extended to services as well as goods. The rational being that the Canadian economy is becoming more and more service-based. Others refuted this suggestion arguing that services are not subject to abuse prior to bankruptcy, since in most cases, they can not be easily liquidated

to meet the debtor's obligations to other creditors.

As a final suggestion, it was proposed to amend the wording of section 81.1 with wording similar to that of section 81.2, in order to confer a form of super-priority which would be applicable to all goods delivered up to 30 or 60 days preceding the date on which the debtor became bankrupt.

It was suggested that the provisions in the BIA which deal with unpaid suppliers be reviewed and/or rewritten as they are presently unworkable and do not afford the intended protection to unpaid suppliers.

2.2. Asset Rollovers

The discussion on **Asset Rollovers**, commonly referred to as "flip-flops" was brief. Although participants did not agree on a definition of what constituted an asset rollover, they did agree that when a company is either bankrupt, under receivership or in the process of being wound-up, asset rollovers can be a good thing, provided the goods in question are acquired, by the new company, at the best market value possible under the circumstances. It was, however, agreed that more transparency is required when these types of transactions occur.

It was agreed that more transparency is needed regarding asset rollovers.

2.3. Receiverships

It was proposed to harmonize federal and provincial legislation dealing with **Receiverships**. Accordingly, it was suggested that the *BIA* be amended to include parallel provisions to that of the provincial legislation which provides for civil sanctions in cases where receivers omit to comply with their duties and/or obligations.

With respect to the issue of non-compliance with the reporting requirements for receiverships under the *BIA*, a large number of participants argued that the cost of complying with said provisions was onerous and cumbersome, particularly for smaller estates. Some creditors argued that if the *BIA* were to require that only trustees be allowed to administer receiverships, the cost of the administration of receiverships would

be affected. One trustee representative commented that the costs of hiring a trustee to administer a receivership prior to the enactment of the 1992 amendments were essentially the same as they were following the coming into force of Part XI. Moreover, it was said that there is very little difference in the costs of administering a receivership versus administering a bankruptcy. The position of the Canadian Insolvency Practitioners' Association (CIPA) on this issue was that all receivers should be licensed trustees, as licenced trustees are accountable not only to their clients, the creditors and the courts, they are also answerable to the CIPA and the OSB.

Unsecured creditors felt that Part XI was of great benefit to them even though they stand to receive very little, if anything, in most receiverships. Part XI was said to assure at least some respectable degree of transparency and the reassurance to creditors, to a certain extent, that their claims are being protected. They argued that more severe penalties should be imposed on those who do not comply with these provisions.

There should be some uniformity or harmonization between federal and provincial legislation dealing with receiverships. As well, it was proposed that more severe penalties be imposed on those who do not comply with these provisions.

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 Bankruptcy and Insolvency Advisory Committee (BIAC) recommendations in April 1997. Having now completed the National Insolvency Forums in 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 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 a long 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 representatives had a number of suggestions. The discussion opened with the topic of **Discharge Hearings**. It was suggested that the *BIA* be amended to introduce a Notice of Intention to Object to a Bankrupt's Discharge. It was further proposed that discharge hearings be held via conference call and/or video-conferencing rather than physical attendance.

Participants agreed that the lack of timeframe with respect to the **Stay of Proceedings** needed to be addressed. Stakeholders reiterated that oftentimes debtors take advantage of the stay of proceedings to dispose of assets in an abusive way. Accordingly, it was proposed to limit the stay of proceedings to nine months.

On the subject of **Proof of Claims**, a number of participants agreed that proof of claims should only be required where a dividend was likely to be distributed to creditors. Alternatively, it was proposed that the statement of affairs be used as *prima facie* evidence of the bankrupt's indebtedness to a creditor, and that the proof of claim be required only in those cases where the creditor did not agree with the amount indicated therein.

Regarding **Student Loans**, participants expressed dissatisfaction regarding the amendment to section 178 of the *BIA* and suggested that the provision be amended to introduce a hardship clause or alternatively provide for mediation.

A few comments was made on the issue of **Consumer Proposals**. Participants suggested that the *BIA* be amended to prohibit related persons from voting for or against a consumer

proposal. It was also proposed that the insolvent person be required to deliver all credit cards to the trustee. Moreover, participants suggested that the existing threshold be increased from seventy-five thousand dollars to two-hundred and fifty thousand dollars and that the consumer proposal regime be applicable to sole proprietorships.

On the subject-matter of **Education**, participants agreed that the OSB should play a prevelant role in developing and implementing a national program geared at educating our youth on the concept of budgeting, credit and financial management.

As a way to streamline the process leading to the issuance of a **Receiving Order**, it was suggested to amend the *BIA* in order to repeal all acts of bankruptcy, except paragraph 42.(1)(j) which provides that "*a debtor commits an act of bankruptcy if he ceases to meet his liabilities generally as they become due*".

With respect to the issue of the **Realization of Assets and the Statement of Affairs**, it was proposed that the *BIA* be amended in order to require trustees to file an amended statement of affairs, which in turn would be forwarded to creditors, in those cases where additional and/or materially significant information was obtained regarding the debtor's assets.

Regarding the issue of **Service Standards**, it was proposed that trustees be required to return phone calls within a specified timeframe (e.g., a day or so).

When asked about the efficiency of our system, corporate and commercial participants commented on the **Taxation of Accounts**. It was proposed that consideration be given to eliminate, in some cases, the current practice of taxing both legal and trustee accounts.

Concerning the issue of **Meetings of Creditors**, it was suggested that they not be mandatory in all cases. However, in those cases where such meetings were necessary, it was suggested that the *BIA* be amended to clearly provide for alternative means of physically attending meetings.

Regarding **Proof of Claims**, participants suggested that the form be revised and simplified and that consideration be given to exempt creditors from filing a proof of claim in certain circumstances.

A number of specific problems were raised with regards to the issue of **Unpaid Suppliers.** For example, the time frame was said to be unpractical and it was mentioned that, in some cases the protection does not apply unless the goods in question are clearly and specifically segregated. It was, therefore, suggested that the provisions of the *BIA* which deal with unpaid suppliers be reviewed and/or rewritten as they are presently unworkable

and do not afford the intended protection to unpaid suppliers.

Moreover, although participants viewed **Asset Rollovers** as an issue of perception, they did agree that more transparency was needed in this regard.

Finally, with respect to the issue of **Receiverships**, participants agreed that both uniformity and harmonization between federal and provincial legislation would be beneficial. It was further proposed that the *BIA* be amended to include more severe penalties for those who omit to comply with the statutory requirements.

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 Saskatoon Conference was well attended and the suggestions for change and improvement to Canada's Insolvency System were very much appreciated.

Thank you, once again.

Summary of Discussion Papers Submitted by Participants

DISCUSSION PAPER #1

Submitted By: The Canadian Bankers Association

CONSUMER BANKRUPTCIES AND 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 AND 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: Gordon Berscheid, Department of Justice of Saskatchewan

STREAMLINING COMPLIANCE WITH BANKRUPTCY DISCHARGE ORDERS - IS MORE NEEDED ?

- Does bankruptcy work efficiently when a Bankrupt makes no effort to comply with a conditional discharge order, choosing instead to retain the status of an undischarged bankrupt? This position is apparently open to a bankrupt given that the duties on conditional discharges provided for in section 176 of the BIA do not require a bankrupt to make a reasonable or any effort to comply with a conditional discharge order.

- Enforcement of the discharge order can be a difficult issue because it may require additional legal and other representation costs as well as additional expense in serving the order on the employer and monitoring compliance thereafter.
- For the Bankrupt who simply will not voluntarily comply with a conditional discharge order, the following are possible measures aimed at enhancing compliance:

  (1) amend section 176 of the Act to provide that Bankrupts have a duty to make reasonable efforts to comply with conditional discharge orders and that failure to comply with that duty is a ground on which the Court may revoke the order of discharge;

(2) expand the authority of the Court by amending section 172 of the Act to provide that it may order a garnishment of the salary, wages or other remuneration by the trustee in the event the Bankrupt is in default in making monthly payments to satisfy a conditional discharge order;

(3) amend section 69.4 of the Act to allow a creditor to apply for a declaration that the stay of proceedings ceases where the Court is satisfied that the Bankrupt has not made reasonable efforts to comply with a conditional discharge order;

(4) expand the bankruptcy offence provisions by amending section 198 of the *Act* to make failure to make reasonable efforts to comply with a conditional order an offence.

DISCUSSION PAPER #5

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.

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 the stakeholders' 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 constraint 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 #6

Submitted By: Professor Tamara Buckwold, College of Law, University of Saskatchewan

RECEIVERSHIPS & PART XI OF THE BIA

- *The interface between Part XI and provincial legislation governing receivership*

The *Personal Property Security Acts* (PPSAs) of all the provinces and territories contain provisions relating to the appointment and conduct of receivers. Both court-appointed and private receivers are required to observe specified accounting and reporting obligations,

along with a general duty of care. Breach by a receiver of any obligation recognized by the PPSA renders him or her liable to any person whose interest in the subject of the receivership is adversely affected by that breach.

The regulatory approach of Part XI of the BIA is in many ways similar to that embodied in provincial legislation, but it appears to adopt a somewhat different emphasis. Provincial legislation recognizes the traditional function of receivership as a security realization device. Receivership law is very much concerned with protection of the proprietary interest of the debtor, while bankruptcy tends to focus on satisfying the claims of creditors.

Part XI obliges receivers to notify all of the debtor's creditors of their appointment, and provide reports to any creditor who requests them. In contrast, the PPSAs make information available to persons who have established an *in rem* claim against the property

subject to the receivership. Unsecured creditors who have not initiated judgement enforcement measures have no entitlement to such information. The BIA thus adds another layer of regulation to the conduct of receiverships, primarily by obliging receivers to provide regular reports to the debtor and to all creditors.

- *The utility of the Part XI reporting* ***reporting requirements***

  Provincial legislation obliges receivers to keep appropriate financial and other accounts, to prepare regular financial statements and to prepare and file a final account of the administration of the receivership. This information must be available to the debtor and to others with an interest in the collateral subject to the receivership, at their request. Provincial law imposes no general requirements of notification or reporting to all of the debtor's creditors comparable to those imposed by sections 245 and 246 of the BIA.

  The notice and reporting requirements of the BIA impose procedural and paperwork obligations on receivers that may be extremely onerous. Those who have proprietary claims against the debtor's assets are in any event entitled to the notices of realization activities prescribed by provincial law. Unsecured creditors have no direct interest in the property subject to the receivership, and in any other context have no right to notification of a secured creditor's realization proceedings. The BIA obliges the receiver to provide unsecured creditors with full reports of his or her administration. Reports must be given to subordinate secured creditors, though their interests are safeguarded by other legislation.

- *Remedial issues*

  The BIA imposes on receivers the same general duty of care as does provincial legislation, and subjects them to a more extensive set of reporting requirements. However, while the debtor or any creditor may obtain court orders of an injunctive nature to compel observance of the Act, there is no provision creating a cause of action for breach of the statutory duties. In contrast, provincial legislation makes a receiver liable for any default in connection with his or her management of the receivership or disposition of collateral. The provincial legislation reflects the common law traditions of receivership, under which the primary device for regulation of a receiver's conduct was his potential legal ability, or in the case of private receivers, the potential liability of the secured creditor appointing him. The BIA seems instead to focus on process and the observance of rules relating to the provision of information.

- *The definition of "Receiver" and the scope of Part XI*

  The definition of "receiver" has raised problems that could easily be resolved by an appropriate amendment. The breadth of the current definition has led some courts to the view that a secured creditor who takes direct action to realize on security is a "receiver" and this is subject to the Part XI reporting requirements if the collateral in question is all or substantially all the debtor's business inventory, accounts receivable or general assets. However, there seems to be no doctrinal or policy justification for subjecting secured

creditors to these additional requirements. Secured creditors realizing against personal property collateral are subject to a comprehensive regulatory scheme under the provincial PPSAs, which promotes efficient realization while protecting other interested parties. Realizations against land invoke provincial foreclosure legislation, which ensures that all interested parties have an opportunity to monitor any disposition. Moreover, secured creditors are subject to both statutory and common law duties of care in the exercise of rights of realization.

- *Conclusions*

Part XI may be criticized to the extent that it functions primarily to impose a set of reporting and notice requirements additional to those that a receiver is already required to observe under provincial law, to little discernable benefit. Ideally, provincial and federal statutes should be rationalized to provide a single set of obligations, standards and procedures applicable to all receiverships.

It is unlikely that the imposition of "higher duties of transparency and accountability" or the development of specific "service standards" would significantly improve the conduct of receivers. They are, under both federal and provincial law, subject to a fairly rigorous duty of care that requires them to balance the interests of all interested parties. However, the creation of a federal cause of action subjecting receivers to personal liability for breach of that statutory duty may alleviate concerns about negligent or inappropriate conduct.

DISCUSSION PAPER #7

Submitted By: Professor Ronald C.C. Cuming, College of Law, University of Saskatchewan

Sections 81.1 and 81.2 of the BIA

- *What is the policy basis of the sections?*

When goods are supplied during a short period prior to invocation of bankruptcy, winding-up or receivership proceedings, in most situations the value of those goods will be part of the estate of the debtor when the trustee or receiver takes control. Unless a special priority for the claims of suppliers is recognized, the enhanced value resulting from the supply of goods will be captured by other creditors of the insolvent business organization. This may be particularly unfair when the beneficiaries of this enhanced value are secured creditors. The policy of section 81.1 is that this value came from an identifiable source and should be returned to that source rather than distributed to other creditors who did not provide it.

- *Should the conceptual approach contained in section 81.2 be applied to all suppliers and all goods?*

Under the approach of section 81.2, the supplier gets a charge on the inventory of the

bankrupt or debtor in receivership. The supplier is not limited to recovery of goods supplies.

- *Is there a compelling policy basis for drawing distinctions between suppliers of goods and suppliers of services when it comes to selecting an appropriate remedy?*

  In many situations both goods and services are supplied to a buyer under a single contract. It would appear anomalous to have one approach to that aspect of the contract applicable to the goods supplier and another approach applicable to that aspect of the contract to the services supplied.

- *What would a "supplier's charge" look like?*

  Give the conceptual basis of a supplier's charge, the charge should protect only claims arising from the supply of goods or services shortly before that bankruptcy or winding-up of the recipient or the appointment of a receiver of its assets. The supplier's charge would have a priority position inferior to that of wage claimants, but superior to their security interest with the exception of purchase money security interests.

- *Effects on other Creditors*

  If a supplier's charge were recognized, unsecured creditors would be affected to the extent that their share of the assets distributable to unsecured creditors would be diminished. Secured creditors, other than those that might be exempted from the charge, would face the risk, upon insolvency of the business organization to which they gave credit, that their security interests would be subject to an unknown number of unpaid supplier claims. There can be no doubt that, in some situations, the availability of a supplier charge would affect the willingness of creditor grantors to provide secured or unsecured credit to business organizations. In order to minimize this effect, it would be necessary to place limits on the amount of a supplier's claim protected by the supplier's charge. A fear that a supplier's charge will have a significant effect on the availability

  credit would be reduced should the Act provide that the charge does not have priority over purchase money security interest.

- *Should there be a Supplier's Charge in Insolvency Proceedings?*

  When the rights of a supplier are limited, as they currently are under section 81.1 of the BIA, to the recovery of goods delivered to a buyer, it is consistent with the policy of our insolvency law that the right of repossession should be stayed when the buyer has made a proposal to remain in business and be exercisable only if the proposal is rejected.

  If the supplier's charge were treated as a security interest, the supplier would be a secured party. As is the case with all secured parties, suppliers would be subject to the stay under sections 69 and 69.1 of the BIA and section 11 of the CCAA. Whether or not suppliers would be placed in a separate voting class because of the special priority they would be

given would be a matter to be determined in the insolvency proceedings.

This approach is justifiable on the basis that their special priority over most secured creditors would be recognized while at the time the ultimate success of an accepted proposal is not jeopardized by suppliers who assert their priority and cause property of the insolvent business organization to be seized and sold.

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