# An Overview of Bankruptcy and Insolvency Law in Canada

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# OVERVIEW OF THE BANKRUPTCY AND INSOLVENCY ACT (“BIA") AND THE COMPANIES CREDITORS ARRANGEMENT ACT (“CCAA")

There are two statutes which set out the law of bankruptcy and insolvency law in Canada. They are the *Bankruptcy and Insolvency Act* (“BIA”) and the *Companies Creditors Arrangement Act* (“CCAA”).

The BIA and the CCAA are very different in approach. The BIA contains 275 sections and is intended to be a complete code for bankruptcies. The CCAA, on the other hand, which deals with corporate restructuring, contains only 22 sections. It allows for flexibility and requires decisions of the court to "fill in the gaps". Whereas much of the law dealing with bankruptcies is within the BIA itself, most of the law dealing with the CCAA is found in judgments.

## A. THE BANKRUPTCY AND INSOLVENCY ACT (“BIA”)

Canadian courts consider the BIA to be a commercial statute, the administration of which is largely in the hands of businessmen. As a result, legal technical positions are not to be given effect to beyond what is necessary for the proper interpretation and administration of the Act.

### 1. Insolvent vs Bankrupt

Pursuant to section 2(1) of the BIA, an "insolvent person" means a person who is not bankrupt, resides or carries on business or has property in Canada, whose liabilities to creditors provable as claims under the BIA amount to at least $1,000, and

(a) is unable to meet obligations as they generally become due;
(b) who has ceased paying current obligations in the ordinary course of business as they generally become due; or
(c) the aggregate of whose property is not, at fair valuation, sufficient to enable payment of all of his obligations, due and accruing due.

## 2. The Purpose of the BIA

The purposes of the BIA include:

(a) permitting an honest but unfortunate individual to obtain a discharge from debts, subject to reasonable conditions, so as to allow the debtor to start again. The financial rehabilitation of an insolvent individual is a fundamental purpose of the BIA;
(b) to provide for the orderly and fair distribution of property of a bankrupt among unsecured creditors on a *pari passu* basis;
(c) to allow for an investigation to be made into the affairs of a bankrupt; and
(d) setting aside of preferences, settlements and other fraudulent transactions.

## 3. Bankruptcy (Receiving) Orders, Assignments and Proposals ( ss. 42-49)

There are three ways a person can become a bankrupt:

(a) a bankruptcy order is made by a Court;
(b) a voluntary assignment into bankruptcy; or
(c) a failed proposal.

### a. Bankruptcy Order

A bankruptcy order, results when one or more creditors file with the court a petition which successfully alleges that:

(a) the debts owing to the petitioning creditor(s) is greater than or equal to $1,000; and
(b) the debtor has committed an act of bankruptcy within six months of the filing of the petition (s. 43).

Section 42 of the BIA defines "acts of bankruptcy" and includes:

(a) an assignment of property to a Trustee for the benefit of creditors;
(b) a fraudulent gift, delivery or transfer of property;
(c) a conveyance or transfer of property (or creation of a charge) that is a fraudulent preference;
(d) the debtor, with the intent to defeat or delay his creditors, departs out of Canada or remains out of Canada or departs from his dwelling or otherwise absents himself;
(e) permitting, for certain periods of time, execution under which the debtor's property is taken;
(f) an admission of his inability to pay debts;
(g) assigns, removes, secretes or disposes of or attempts or is about to do same with his property with the intent to defraud, defeat or delay his creditors or any f them;
(h) giving notice to creditors that the debtor has suspended or is about to suspend payment of debts;
(i) defaulting on a proposal; and
(j) if the debtor ceases to meet liabilities generally as they become due.

The most commonly relied on act of bankruptcy is ceasing to meet liabilities generally as they become due. However, the creditors must point to a pattern of failing to meet liabilities, as opposed to a failure to pay one creditor. Special circumstances may, however, exist such that failure to pay one creditor is an act of bankruptcy, for example, if that creditor is owed a significant sum of money.

If a bankruptcy order is made, a Trustee must be appointed over the property of the bankrupt.(s. 43(9)).

The Court may, if it is shown to be necessary for the protection of the estate of a debtor, at any time after the filing of a petition for a bankruptcy order but before the bankruptcy order is made,

appoint a licensed trustee as interim receiver of the property of the debtor or any part thereof. The general idea of an interim receiver is to secure and protect property of a debtor, pending the hearing of the petition (s. 46).

**b. Voluntary Assignment**

An insolvent person, pursuant to section 49 of the BIA, may make an assignment of all of his property for the general benefit of his creditors. This is done by filing an assignment with the Official Receiver. The official receiver then appoints the Trustee.

**c. Annulment**

Section 181(1) of the BIA allows the Court to annul a bankruptcy where, in the opinion of the Court a bankruptcy order ought not to have been made or an assignment ought not to have been filed.

**d. Proposals (ss. 50-66.4)**

A proposal pursuant to the BIA is a court sanctioned proposal to creditors.

A proposal may be made by an insolvent person, a receiver with respect to an insolvent person, a liquidator, a bankrupt or a Trustee (s. 50(1)).

Upon the filing of a NOI or a proposal, a general stay comes into effect against creditors, including secured creditors to which the proposal is made (s. 69).

A proposal can occur after bankruptcy, in which case the bankruptcy is "suspended" pending the out come of the proposal.

A proposal may be made to all creditors of a debtor including secured creditors. In this regard, a proposal is different from a bankruptcy. A proposal can affect the rights of a secured creditor.

Further, during the course of proposal proceedings, the debtor retains control over his assets and business.

Proposal proceedings are started by the insolvent person/bankrupt lodging with a Trustee a written proposal, together with documentation regarding financial affairs (s. 50(2)). If a proposal is made by a bankrupt, it must be approved by the inspectors before further action is taken. For proposals made in respect of an insolvent person, the Trustee is to file a copy of the proposal with the Official Receiver (s. 62). When filing a proposal, the Trustee is to file a cash flow statement.

An insolvent person may file a "notice of intention to make a proposal" (“NOI”) with the Official Receiver prior to lodging a proposal. Within 10 days after filing the NOI, the insolvent person is to file with the Official Receiver a projected cash flow statement, a report on the reasonableness of the cash flow statement prepared by a Trustee and a report containing certain representations. This allows the insolvent person time to prepare the proposal.

The proposal is supposed to be filed within 30 days after the NOI is filed, but it is possible to apply to the Court for extensions not exceeding, in the aggregate, five months after the expiration of the initial 30-day period (s. 50.4(9)).

A proposal or NOI must contain the consent of a Trustee who is to be the Trustee for that proposal.

A proposal does not prevent a secured creditor to whom the proposal has not been made from immediately realizing on that security (s. 69.1(5)).

Once a proposal is filed with the Official Receiver, the Trustee is to call a meeting of the creditors within 21 days. It is possible, however, for such a meeting to be adjourned pending further investigation and examination (ss. 51-52).

At the meeting of creditors, all classes of creditors are entitled to vote. The proposal is deemed to be accepted by the creditors if, and only if, all classes of unsecured creditors vote for the acceptance of the proposal by a majority number and two-thirds in value present, personally or by proxy, and voting (s. 54).

Secured creditors are only bound by the terms of a proposal if the relevant class of secured creditors votes in favour of the proposal, again, majority in number, two-thirds in value, of creditors present and voting.

Where a proposal is rejected by creditors in respect of an insolvent person, the insolvent person is deemed to have made an assignment in bankruptcy at the time he filed the proposal or NOI (s. 57).

If a proposal is accepted, the Trustee must apply to the Court for approval of the proposal. The Court can refuse to approve a proposal when it is of the opinion that the terms of the proposal are not reasonable or not calculated to benefit the general body of creditors (ss. 58-59).

Proposals must provide for payment in priority of certain claims, including the fees and expenses of the Trustee and Crown claims (s. 60). No proposal in respect of an employer shall be approved by the Court unless it provides for payments to employees equal to the amount such employees would be qualified to receive under section 136(l)(d) of the BIA if the employer became bankrupt and the court is satisfied the employer can and will make such payments (s. 60(1.3)).

The Court’s approval of a proposal made after bankruptcy operates to annul the bankruptcy and to vest in the debtor or such other person as the Court may approve all the right, title and interest of the Trustee in the property of the debtor unless the terms of the proposal otherwise provide (s. 61).

A proposal accepted by creditors and approved by the Court is binding on the creditors in respect of all unsecured claims and in respect of secured claims which the proposal addressed and where such class of the secured creditors voted for the proposal (s. 62(2)).

Where one or more classes of secured creditors vote against a proposal, a secured creditor holding a secured claim in such a class may then realise on or otherwise deal with that security (s. 69.1(6)).

If the Court does not approve a proposal then the insolvent person is deemed to have made an assignment in bankruptcy (s. 69.1(2)(a)).

If there is a default in performance of the proposal and the default is not waived by the inspectors/creditors or remedied, then an application must be made to the Court and the Court may annul the proposal, in which case the debtor shall be deemed to have immediately made an assignment in bankruptcy (s. 63).

In order to allow for effective voting on a proposal, the proposal must provide for sorting out claims, classes of creditors, and meeting procedures including voting. Any interested party can apply to the Court for directions in this regard.

A consumer proposal may be made by a consumer (individual) debtor, who is bankrupt or insolvent and whose aggregate debts, excluding any debts secured by the person's principal residence, do not exceed $75,000. The purpose of the consumer proposal sections is to permit such proposals to be handled quickly, efficiently and with a minimum of administration and expense. Such proposals are carried out within a narrow time frame and can propose a settlement of debts, an extension of time for payment, or both.

## 4. Stay of Proceedings (ss. 69-69.5)

Upon bankruptcy, no creditor has any remedy against the debtor or the debtor's property or shall commence or continue any action, execution or other proceedings for the recovery of a claim movable in bankruptcy, until the Trustee has been discharged (s. 69.3(1)).

However, it is a general principle of the BIA that secured creditors are not affected by a bankruptcy. Secured creditors are not subject to the stay and are not prevented from realizing or otherwise dealing with security unless a court otherwise orders (s. 69.3(2)).

A creditor affected by a stay may apply to the court for an order that the stay not apply in whole or in part to such creditor. This provision is meant to allow creditors to, for example, commence actions either to preserve limitation periods or to take advantage of insurance that a bankrupt might have (s. 69.4).

Section 69 also provides for a stay with respect to proposals.

**5. Property of the Bankrupt (ss. 67-101.2)**

On bankruptcy, the bankrupt ceases to have any ability to dispose of or otherwise deal with his property and subject to the BIA and to the rights of secured creditors, the property passes to and vests in the Trustee (s. 71(2)).

All property of the bankrupt passes to the Trustee except:

(a) property held by the bankrupt in trust for any other person; and
(b) property that as against the bankrupt is exempt from execution or seizure under any laws applicable in the province and within which the property is situated and within which the bankrupt resides (s. 67).

Property which is acquired by a bankrupt after the date of bankruptcy but prior to discharge forms part of the estate of the bankrupt and is divisible amongst creditors.

A bankruptcy order/assignment takes precedence over attachments, garnishments, judgments, etc., except those that have been completely executed by the payment to the creditor prior to the bankruptcy. In other words, the Trustee has a superior right to any assets subject to such garnishment or judgment unless the process is completed prior to bankruptcy (s. 70).

If a person has a claim over property which was in the possession of the bankrupt at the time of bankruptcy, to pursue such claim the person must file with the Trustee a proof of claim in the appropriate form (s. 81). The Trustee will consider the claim and make a decision. The decision of the Trustee may be appealed to the Court.

The BIA provides rights for unpaid and unsecured suppliers to repossess goods. To take advantage of this section of the BIA, an unpaid supplier must fit strictly within that section. Where a supplier has sold and delivered goods to a purchaser for use in relation to the purchaser's business, the supplier may repossess the goods if:

(a) the supplier makes a written demand for repossession to the purchaser, trustee or receiver within 15 days after the day on which the purchaser became bankrupt or became a person who is subject to a receivership;

(b) the goods were delivered within 30 days before the day on which the purchaser became bankrupt or became a person who is subject to a receivership;

(c) at the time when the demand is presented, the goods

  (i) are in the possession of the purchaser, trustee or receiver,

  (ii) are identifiable as the goods delivered by the supplier and are not fully paid for;

  (iii) are in the same state they were on delivery;

  (iv) have not been resold at arm's length; and

  (v) are not subject to any agreement for sale at arm's length; and

(d) the purchaser, trustee or receiver does not, forthwith after the demand, pay the balance owing. (s. 81.1)

The supplier's right to repossess goods expires if not exercised within 10 days after the purchaser, trustee or receiver presents the supplier with a written notice admitting that right, unless there is an extension by agreement.

## 6. Settlements and Preferences (ss. 91-106)

The BIA provides a Trustee with powers to set aside certain transactions where the assets of the bankrupt have been transferred to third parties prior to bankruptcy.

Pursuant to section 91 of the BIA, any "settlement" of property made within one year of the "date of the initial bankruptcy event" is void as against the Trustee.

Pursuant to section 2 of the BIA, the "date of the initial bankruptcy event" means:

(a) the date of the filing of an assignment;
(b) the date of the filing of a proposal or notice of intention; or
(c) the date of the filing of the petition where a receiving order is made.

Any settlement of property made within five years of the initial bankruptcy event is void as against the Trustee if the Trustee can prove that the settlor was, at the time of the settlement, unable to pay all the settlor's debt without the aid of the property in question (s. 9l(2)). Section 91 of the BIA does not apply to settlements made in good faith and for valuable consideration.

Where a person engaged in business makes an assignment of existing or future book debts and subsequently becomes bankrupt, the assignment is void as against the trustee with respect to any book debts that have not been paid at the date of bankruptcy (s. 94). However, this section does not apply to an assignment of book debts that is registered pursuant to a statute of the province if the assignment is otherwise valid in accordance with the law of the province. Further, this section does not render void an assignment of book debts due at the date of the assignment from specified debtors or debts becoming due under specified contracts or an assignment of book

debts included in a transfer of business made in good faith and for adequate valuable consideration.

Section 95 of the BIA provides that any conveyance, property transfer, charge made on property, payment, obligation incurred and judicial proceeding taken or suffered by an insolvent person in favour of any creditor with a view to giving that creditor a preference over other creditors is, when made within three months before the date of the initial bankruptcy event, deemed fraudulent and void as against the trustee. When any such transaction has the effect of giving a creditor preference over other creditors, it shall be presumed to have been made with a view to giving the creditor preference as long as it occurred within three months of the initial date of bankruptcy.

The three-month period mentioned above is one year where the transaction is in favour of a person related to the insolvent person (s. 96).

In order to successfully invoke this section, the Trustee must establish a fraudulent intent, that is, a view to prefer, on the part of the debtor. Proof of concurrent intent, that is, on the part of the preferred creditor, is unnecessary. However, it can be difficult to establish fraudulent intent and so the question of whether the presumption in section 95 of the BIA applies, that is, the three-month rule, is often critical to the outcome of the case.

Pursuant to section 97 of the BIA, no payment, delivery, conveyance, transfer, contract, dealing or transaction by a bankrupt made between the date of the initial bankruptcy event and the date of the bankruptcy is valid except for a payment to a creditor, a payment or delivery to the bankrupt, a conveyance or transfer for adequate valuable consideration or a transaction, including the giving of security, for adequate valuable consideration. The "exceptions" are valid, if made in good faith, subject to the provisions of the Act dealing with settlements, preferences and reviewable transactions.

However, after-acquired property is different inasmuch as pursuant to section 99 of the BIA, until the Trustee intervenes, transactions regarding such property by an undischarged bankrupt

with a person dealing with the bankrupt in good faith and for value in respect of such property are valid and the person acquiring such property from the bankrupt receives good title.

Pursuant to section 100 of the BIA, where a bankrupt has sold, purchased, leased, hired or supplied or received property or services in a reviewable transaction within one year of the date of the initial bankruptcy event, the Trustee may inquire as to whether the bankrupt received fair market value and may commence proceedings for the difference between the fair market value the bankrupt ought to have received and any consideration the bankrupt did receive where the Court finds that the consideration the bankrupt received was "conspicuously greater or less than the fair market value of the property or services concerned".

## 7. Administration of the Bankrupt’s Estate (ss. 102-157)

The BIA allows creditors a substantial role in the administration of a bankrupt's estate.

In order for a creditor to be entitled to vote at meetings of creditors or to share in any distribution, the creditor must file a proof of claim (s. 124).

Secured creditors may also file a proof of claim for the unsecured balance of any amount owing to the secured creditor. The secured creditor may prove the entire claim if the secured creditor surrenders his security to the trustee for the general benefit of the creditors (ss. 112 and 127).

### a. First Meeting of Creditors

Within 5 days of the appointment of the Trustee, the Trustee must send a notice to all known creditors of the bankruptcy and of the first meeting of creditors to be held within 21 days following the Trustee's appointment (s. 102). The meeting date can be changed.

The procedure to be followed by the Trustee prior to the first meeting of creditors is as follows:

(a) the Trustee must file a bond required by the bankruptcy order, or in the case of an assignment, by the Official Receiver's certificate;

(b) the Trustee may request that any mail to the bankrupt be redirected to the Trustee;

(c) the Trustee is to take possession of the books of the bankrupt and make an inventory of assets;

(d) the Trustee is to prepare a statement of affairs for the bankrupt;

(e) the Trustee must ensure that the property of the bankrupt and the assets are stored in a safe place;

(f) the Trustee must set up a trust account for the bankruptcy;

(g) the Trustee must establish proper books to show money received and money disbursed;

(h) within 5 days after his appointment, the Trustee must send the notice regarding the first meeting of creditors to the creditors and the bankrupt. With this notice you will be sent a list of creditors as well as a proof of claim form;

(i) in the case of the bankruptcy of an individual, the Trustee must set out in the notice calling such meeting information concerning the financial situation of the bankrupt and the obligation of the bankrupt to make payments under section 68 of the BIA;

j) as soon as possible, and in any event not later than 5 days prior to the first meeting of creditors, notice of the bankruptcy and the first meeting must be published in a local newspaper;

(k) the Trustee and bankrupt must attend for an examination of the bankrupt at the time fixed by the official receiver.

At meetings of creditors, the Official Receiver, or his nominee, that is the Trustee, is chairman (s. 105). A quorum is one creditor entitled to vote (s. 106).

At the first meeting of creditors:

(a) the actions of the Trustee to date, including the statement of affairs and examination of the bankrupt are tabled;

(b) the Trustee will be confirmed or else there will be a motion to appoint a new Trustee;

(c) there will be an appointment of one to five "inspectors" who are creditors and are nominated and elected by creditors, pursuant to section 116 of the BIA; and

(d) there will be a discussion of the affairs of the bankrupt, including an opportunity by the creditors to question the bankrupt or an officer of a bankrupt corporation.

**b. Inspectors**

Following the election of inspectors, they are the ones who instruct the Trustee by majority as to further steps to take. The Trustee will vote in the case of a tie (s. 117(2)).

After the first meeting of creditors, it is not unusual for there to be no other meetings of creditors. The Trustee may carry out the remainder of the administration of the estate as instructed by meetings of inspectors. At the end of the administration of the estate, the Trustee will send correspondence to the creditors outlining what has occurred and hopefully providing a distribution.

**c. Provable Claims**

Pursuant to section 121 of the BIA, all debts and liabilities, present or future, to which a bankrupt is subject on the day of bankruptcy or to which the bankrupt may become subject before discharge by reason of any obligation incurred before the bankruptcy are deemed to be claims provable under the BIA. For contingent or unliquidated claims, a determination as to whether such claim is a provable claim and, if so, a valuation must be made in accordance with section 135 of the BIA.

Under section 135 of the BIA, the Trustee who receives a proof of claim must make a determination as to whether the claim is accepted and may disallow in whole or in part any claim, right to priority or security. A determination by a Trustee may be appealed to the Court.

**d. Examination of the Bankrupt**

A significant right granted to a creditor by the BIA is whereby on application to the Court, by a creditor, or other interested person, and on sufficient cause being shown, the Court may order the examination of the bankrupt or any other person for the purpose of investigating the administration of the bankrupt estate.

**e. Distribution**

Generally, the role of the Trustee is to gather, secure and sell the estate of the bankrupt. Proceeds are then to be distributed to unsecured creditors.

Section 136 of the BIA sets out a scheme or priority of distribution of net proceeds in the following order:

(a) in the case of a deceased bankrupt, the reasonable funeral and testamentary expenses;
(b) the costs of administration;
(c) the levy payable under section 147 of the BIA to the Superintendent of Bankruptcy;
(d) wages for services rendered to the bankrupt during six months immediately preceding the bankruptcy to a maximum of $2,000 per person;
(e) municipal taxes for two years immediately preceding the bankruptcy, not exceeding the value of the interest of the bankrupt in the property in question;
(f) to landlords for arrears of rent for a period of three months immediately preceding the bankruptcy and accelerated rent for a period not exceeding three months following the bankruptcy, if called for under the lease, subject to a limit being the value of the property of the bankrupt on the premises under lease;
(g) costs incurred by a creditor for asset seizure underway at the date of bankruptcy, but only to the extent of the value of the property exigible thereunder;
(h) other claims for statutory deductions.

After the payment of these "preferred claims", all claims proved in a bankruptcy are to be paid rateably (s. 141).

A bankrupt is entitled to receive any surplus in the estate (s. 144).

**f. Duties of the Bankrupt**

The duties of a bankrupt are as follows:

(a) make discovery of and deliver all property under his possession or control to the Trustee;
(b) deliver all credit cards to the Trustee;
(c) deliver to the Trustee all books, records, documents, writings and papers in any way relating to his property or affairs;
(d) attend before the Official Receiver for an examination under oath with respect to conduct, causes of bankruptcy and disposition of property;
(e) prepare and submit to the Trustee a statement of the bankrupt's affairs;
(f) make or give all assistance within his power to the Trustee, including making an inventory of assets;
(g) disclose to the Trustee all property disposed of within one year before the date of the initial bankruptcy event;
(h) disclose to the Trustee all property disposed of by gift or settlement without adequate valuable consideration within five years of the date of the initial bankruptcy event;
(i) attend the first meeting of creditors, unless prevented by sickness or other sufficient cause;
j) when required, attend other meetings of creditors or inspectors or with the Trustee;
(k) submit to such other examinations under oath with respect to his property or affairs as required;

(l) aid to the utmost the realization of his property and distribution of proceeds among creditors;
(m) execute such powers of attorney, conveyances, deeds and instruments as required;
(n) examine the correctness of all proofs of claim filed if required;
(o) immediately disclose to the Trustee knowledge of any false claim filed;
(p) inform the Trustee of any material change in his financial situation;
(q) carry out such acts as may be reasonably required by the Trustee or directed by the court; and
(r) until discharge, keep the Trustee advised of his place of residence.

Pursuant to section 59, where the bankrupt is a corporation, an officer of the corporation or a person who has had control in fact is to attend before the Official Receiver for an examination and perform all of the duties imposed on the bankrupt by the BIA.

**8. Discharge of the Bankrupt (ss. 168.1-182)**

In the case of a first time individual bankrupt, section 168.1 of the BIA applies. In that situation:

(a) the Trustee shall, before the expiration of an eight-month period immediately following the date of bankruptcy, file a report and send a copy to the bankrupt and to creditors who have requested a copy;
(b) if anyone intends to oppose the discharge of the bankrupt, notice must be given to the Superintendent, Trustee and bankrupt;
(c) if notice of opposition is given, the Trustee is to forthwith apply to the Court for an appointment for a hearing of the opposition; and
(d) where none of the Superintendent, Trustee or creditor gives notice of opposition to the discharge in the nine-month period immediately following the bankruptcy, then at the end of that nine-month period, the bankrupt is automatically discharged.

In any other case, a bankrupt must apply for a discharge.

The bankruptcy itself operates as an application for discharge unless the bankrupt is a corporation or the bankrupt in writing waives this application. If no notice of waiver is served on the Trustee, the Trustee must, not earlier than three months and not later than one year following the bankruptcy, apply to the court for an appointment for a hearing of the application of discharge. There is a notice to creditors of any such application.

A bankrupt corporation may not apply for a discharge unless it has satisfied the claims of its creditors in full.

With respect to the discharge application, the Trustee must prepare a report on the affairs of the bankrupt, causes of bankruptcy, the manner in which the bankrupt performed his duties, the conduct of the bankrupt, offences under the BIA and any other fact, matter or circumstance that would justify a court in refusing an unconditional order of discharge.

The Trustee’s report is to be accompanied by a resolution of inspectors declaring whether or not they approve or disapprove of the report (s. 170). This report is filed in court prior to the discharge application, copied to the Superintendent to the bankrupt and to each creditor who requests a copy. Creditors who intend to oppose a discharge on grounds other than those in the Trustee's report must give notice to the Trustee and bankrupt (s. 170(7)).

Pursuant to section 172 of the BIA, the Court may

(a) grant or refuse an absolute order of discharge;
(b) suspend the operation of the order for a specified time; or
(c) grant an order of discharge subject to any terms or conditions with respect to any earnings or income that may afterwards become due to the bankrupt or with respect to after-acquired property.

Pursuant to section 172(2) of the BIA, the Court shall upon proof of the facts mentioned at section 173:

(a) refuse the discharge of a bankrupt;
(b) suspend the discharge for such period as the court thinks proper; or
(c) require the bankrupt, as a condition of his discharge, to perform such acts, pay such monies, consent to such judgments or comply with such other terms as the court may direct.

The facts for which a discharge may be refused, suspended or granted conditionally in section 173 are:

(a) assets of the bankrupt are not of a value equal to 50 cents on the dollar on the amount of the bankrupt's unsecured liabilities
(b) the bankrupt has omitted to keep such books of account as are usual and proper in the business carried on by the bankrupt;
(c) the bankrupt has continued to trade after becoming aware of being insolvent;
(d) the bankrupt has failed to account satisfactorily for any loss or deficiency of assets;
(e) the bankrupt brought on the bankruptcy by rash and hazardous speculations, unjustifiable extravagance, gambling or culpable neglect of his affairs;
(f) the bankrupt has put any creditors to unnecessary expense by frivolous or vexatious defences;
(g) the bankrupt has, within three months of the date of the initial bankruptcy event, incurred unjustifiable expenses by bringing frivolous or vexatious actions;
(h) the bankrupt has, within three months before the date of the initial bankruptcy event, given an undue preference to a creditor;
(i) the bankrupt has, within three months before the date of the initial bankruptcy event, incurred liabilities resulting in the bankrupt's assets being equal to 50 cents on the dollar on the amount of the bankrupt's unsecured liabilities;
(j) the bankrupt has on any previous occasion been bankrupt or made a proposal;
(k) the bankrupt has been guilty of any fraud or fraudulent breach of trust;
(1) the bankrupt has been guilty of any offence under the BIA;

(m) the bankrupt has failed to comply with a requirement to pay;

(n) the bankrupt chose bankruptcy rather than a viable proposal; and

(o) the bankrupt has failed to perform the duties imposed on the bankrupt under the BIA or to comply with any order of the court.

Pursuant to section 178(1) of the BIA, an order of discharge does not relieve the bankrupt from:

(a) any fine, penalty or restitution order imposed by a court in respect of an offence;

(b) any judgment with respect to intentional harm, sexual assault or wrongful death therefrom;

(c) any debt for alimony;

(d) any debt for support, maintenance or an affiliation order;

(e) any debt or liability for fraud, embezzlement or misappropriation;

(f) any debt or liability for obtaining property by false pretences or fraudulent misrepresentation;

(g) liability for the dividend that a creditor would have been entitled to receive on any provable claim not disclosed to the Trustee, unless the creditor had notice or knowledge of the bankruptcy and failed to take reasonable action to prove its claim;

(h) any debt or obligation in respect of a loan made under the Canada Student Loan Act or similar legislation.

Subject to sections 173 and 178, an order of discharge releases the bankrupt from all claims provable in bankruptcy.

Where a bankrupt fails to perform duties imposed after discharge or it appears to the Court that the discharge was obtained by fraud, the Court may annul the discharge (s. 180).

## 9. Comparison of Personal and Corporate Bankruptcy

The BIA does not generally seek to distinguish between corporate and consumer bankruptcies.

Generally, the BIA operates the same for both companies and individuals. There are, however, a few differences, including:

(a) the simplified "consumer proposal" and “summary administration” is only available to individuals;

(b) an issue can arise with corporations as to who is entitled to make a decision to make an assignment if a receiver has been appointed. Generally, a receiver of a company must seek leave of the court to make a voluntary assignment into bankruptcy. This situation does not occur with an individual;

(c) with respect to the estate of a bankrupt, for individuals certain property is exempt from seizure under provincial legislation and thus exempt from distribution to creditors. This is not the case with companies;

(d) individual bankrupts are entitled to keep a portion of income earned to maintain a reasonable standard of living, in accordance with standards set by the Superintendent of Bankruptcy. Any income in surplus of such standard must be paid to the Trustee;

The BIA is not designed to give companies "a fresh start". On the other hand, first-time individual bankrupts are automatically discharged (if there is no opposition) after nine months, and all individual bankrupts will eventually be discharged, although perhaps with conditions attached.

## B. COMPANIES CREDITORS ARRANGEMENT ACT (“CCAA”)

The CCAA permits compromises or arrangements to be made between an insolvent company and its creditors, both unsecured and secured (or one or more classes of such creditors).

The CCAA has a broad remedial purpose, namely, giving a debtor company an opportunity to find its way out of financial difficulties short of bankruptcy, foreclosure or the seizure of assets through a receivership.

The purpose of the CCAA is to provide the debtor with an opportunity to find a plan which will enable the debtor to meet the demands of creditors in some fashion, whether refinancing with new lending, equity financing, the sale of part or all of the business as a going concern or some other method.

The essential element to the CCAA is the concept of a re-organizational "plan" to which the debtor and its creditors agree.

The CCAA is intended to:

(a) permit an insolvent company to avoid or be discharged from bankruptcy by making a compromise or arrangement with its creditors;
(b) permit the company to remain in business notwithstanding that it is insolvent;
(c) protect an insolvent company for a time from proceedings by creditors which would prevent it from carrying out the terms of a compromise or arrangement;
(d) protect the interests of creditors and to permit an orderly distribution of the debtor company's assets;
(e) maintain the status quo for a period while the insolvent company attempts to gain the approval of its creditors for a proposed arrangement which will, enable the company to remain in operation for the future benefit of the company and its creditors;

(f) permit equal treatment of creditors of the same class;

(g) preserve the insolvent company as a viable operation and to reorganize its affairs to the benefit not only of the debtor, but of the creditor; and

(h) provide a structured environment in which large insolvent companies can continue to carry on business and retain control over their assets while their creditors, shareholders and the court consider a plan or compromise.

The rights of creditors under the CCAA cannot be compromised unless:

(a) the creditor has been given a right to vote in the appropriate class on the proposed plan;

(b) the creditor's vote is in accordance with a value ascribed to the claim by Court approved procedures;

(c) the class in which the creditor has been appropriately placed votes, by majority in number and two-thirds in value of the creditors present, in favour of the plan; and

(d) the court has sanctioned the plan on the basis that it is fair and reasonable, with considerable deference being given by the Court in this regard to the votes of creditors.

There is nothing in the CCAA which exempts any creditors of a debtor company from its provisions.

In contrast with sections 178 and 179 of the BIA which are preoccupied with the competing rights and duties of the borrower and the lender, the CCAA serves the interests of a broad constituency of investors, creditors and employees.

Generally, smaller, less complicated corporate restructuring will be done by proposal. Larger, more complex restructuring will be done under the CCAA.

**a. Application of the CCAA**

The CCAA is available to any Canadian company, except for banks, railway or telegraph companies, insurance companies or trust and loan companies.

In order to seek relief under the CCAA, a company must be a "debtor company", meaning the company:

(a) is bankrupt or insolvent;
(b) has committed an act of bankruptcy within the BIA or is deemed insolvent under the *Winding-up and Restructuring Act*; or
(c) is in the course of being wound up under that Act because the company is insolvent .

Perhaps most importantly, the CCAA only applies in respect of a debtor company or affiliated debtor companies where the total of the claims exceeds $5 million.

**b. The Stay of Creditors**

The first step in most CCAA proceedings is an application for a general stay pursuant to section 11 of the CCAA.

In British Columbia, a CCAA proceeding is brought by petition and to obtain the first order the "initial application" is usually brought without notice. The order will give creditors and other interested parties leave to appear and argue the appropriateness of the initial order.

The affidavit filed with the petition will set out the corporate structure, the business and background to the company, the assets and liabilities of the company, the reasons for the financial difficulties and a basis for a plan of restructuring.

The initial application must include a projected cash flow statement and copies of financial statements for the year prior (if there were no statements prepared in the year prior, a copy of the most recent statements).

The initial stay order is for a period of 30 days, at which point the petitioner must apply for an extension.

In British Columbia, the practice is for one Judge of the Supreme Court to become seized of a CCAA proceeding.

Section 1l(6) sets out the burden of proof on the applicant for an initial stay order or extension as being:

(a) the applicant must satisfy the court that circumstances exist that make such an order appropriate; and
(b) in the case of an application for an extension, the applicant must satisfy the court that the applicant has acted, and is acting, in good faith and with due diligence.

The threshold for an initial stay order is not high if the CCAA otherwise applies. One factor the Court will consider is whether or not there is any hope of a restructuring. Another factor is whether or not there is a business to be saved.

There are many issues which can arise with respect to a stay order including:

(a) scope of the stay;
(b) whether or not persons who supply goods or services to the debtor are to continue to do so and, if so, on what terms;
(c) position of directors and officers;
(d) sale of significant assets prior to consideration of a plan by a meeting of creditors;
(e) generally, security of assets pending the end of the CCAA proceeding;
(f) debtor in possession financing;

(g) role of the monitor;

(h) priority for professional and monitor fees; and

(i) petitioner's obligations to report to the monitor, court and creditors.

In order for a court to authorize debtor in possession financing, there must be cogent evidence that the benefits of the financing clearly outweigh the prejudice to lenders whose security is being subordinated to the financing.

It is necessary for the Court when making an order pursuant to section 11 to appoint a "monitor" to monitor the business and financial affairs of the petitioner. The monitor is an officer of the Court and will be directed by the Court. A monitor is to have access to all of the company's records, file reports with the court (on notice to creditors) with respect to the company's ongoing business and financial affairs, and carry out such other actions as the court may direct, including, usually, being involved with and assisting in the formulation of the plan. Normally, the fees of the monitor and its legal counsel are granted a first priority on all of the assets of the petitioner(s).

In addition to a monitor, the Court can appoint an interim receiver and a restructuring officer or committee.

Compromises and Arrangements

Pursuant to sections 4 and 5 of the CCAA, a petitioner may, on application to the Court, obtain an order from the Court requiring a meeting of the creditors or classes of creditors (and possibly shareholders) to consider a plan of restructuring.

Usually in a contested CCAA proceeding, this application is several months after the initial stay order, once the petitioner(s) has had a chance to assess its options, find additional financing, partners or buyers, negotiate with creditors and put together a draft plan. In an uncontested CCAA proceeding, where creditors are not opposing, there may well be no initial stay order at all and the application for an order calling a meeting may be the first order applied for.

If the evidence placed before the Court indicates there is no reasonable chance that the petitioner will be able to continue to operate its business or that the plan is doomed to failure, the Court may refuse to order a meeting of creditors and dismiss the application and probably the proceeding.

At any time an interested party can bring an application to lift the stay (either generally or in part) and dismiss the proceeding. The test, however, is a high one, and the creditor must show either ongoing prejudice or that the proceeding and any proposed plan are "doomed to failure". As a matter of common sense, as time goes on, the chances of a successful restructuring occurring usually will diminish, and the chances therefore of a successful application to lift the stay are enhanced.

If the Court orders that a creditors/shareholders meeting occur, the order must deal with the procedural issues regarding the meeting. There must be determination of claims and the amount of claims, as well as a claims barring procedure after a certain point (s. 12).

Generally, if a creditor is dissatisfied with how a petitioner deals with its claim, it will have the right to apply to the Court. There must also be terms setting up the meeting, dealing with notice of the meeting, proxies and the procedure for voting. Normally, the monitor deals with such matters.

An important issue in any proposed plan is the division of creditors into classes.

In order for a plan to be endorsed by creditors at the meeting, there must be a majority in number representing two-thirds in value of the creditors in each class of creditors, present at a meeting who vote in favour of the plan (s.6).

If a proposed plan is looked on favourably by some creditors but not others, there are tactical decisions to be made regarding how creditors are to be divided up into classes.

Generally, however, creditors of the same characteristics and circumstances must be put in one class and treated equally.

If the requisite number of creditors have voted in favour of the plan, the next step is for the petitioner(s) to apply to court for approval of the plan. A court is not bound by the decision of the creditors and must decide, independently, whether, in the court's view, the plan is fair and reasonable. Fair and reasonable does not necessarily mean equal, it means equitable and fair.

In determining whether a plan is fair and reasonable, the following are relevant considerations for the Court:

(a) The composition of the unsecured vote. The vote must be properly classified. There must be no secret arrangements to give an advantage to one creditor or creditors. The approval of the plan by the requisite majority of creditors is most important;
(b) Anticipated receipts in liquidation or bankruptcy. It is helpful if someone independent (for example, the monitor) has prepared a comparative liquidation analysis;
(c) Alternatives to the plan. Evidence that other options have been explored and rejected as unworkable is useful;
(d) Oppression of rights of certain creditors;
(e) Unfairness to shareholders; and
(f) Public interest. For example, retention of jobs for employees and support of the plan by the company's unions.

If a plan is rejected no consequences automatically follow. If there is a possibility for an alternative plan, the proceeding may continue. If, on subsequent application, the stay is lifted and the proceeding is ended by Court Order, creditors can then take whatever steps are available to them.

When a plan has been sanctioned by the court, it is binding on all creditors affected by the plan.