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Annual Review of Insolvency Law

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11 — Employee Protection In Insolvency Proceedings — Reviewing the Performance And Setting The Objectives

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I. — Introduction

One of the principal objectives of the modifications made to the Canadian insolvency laws[FN2] was to enhance the protection of employees in the event of the insolvency of their employer. Some of the employee protection provisions came into effect in July 2008, while the remainder came into effect in September 2009.

Considering that some of these provisions have now been in effect for more than two years, it is time to review their performance, as compared with the intentions when they were designed, and whether any specific problems have surfaced in their application or interpretation.

This paper seeks to review the practical problems that have surfaced to date and how these problems are being addressed. Part I explains the historical background of the provisions implemented to protect employees and outlines the features of this protection. Parts II to VI outline the specific problems that have surfaced to date, how these affect the administration of estates, and in the cases where the Court has been asked to intervene, the solutions developed through jurisprudence. Part VII outlines the proposed new legislation that is currently being considered by Parliament to further enhance the protection of employees in an insolvency situation. Part VIII concludes with a note of caution that while protection of employee rights is a worthwhile endeavour, we should be mindful to avoid going overboard and thereby create practical problems that may have unintended impacts on the economy as a whole.

II. — A Bit of History

The latest set of revisions to the Canadian insolvency laws went through a long and difficult path before coming into effect. The revision process started in time for the five year mandatory review that had been built into the statutes in 1997;[FN3] then continued with an in-depth consultation process and study of the legislation by the Standing Senate Committee on Banking, Trade and Commerce. That study culminated in the preparation of a de-

tailed report on recommended changes.[FN4] Draft legislation was finally tabled in June 2005,[FN5] and the customary review process by Parliament was initiated. Despite the fact that several parties made representations that the draft legislation contained serious flaws,[FN6] the review process was cut short,[FN7] with very little changes made to the Bill. The legislation received a very rapid approval by Parliament and the Senate and received Royal assent in the last few days of the 38th Parliament.[FN8] While the Bill received Royal Assent, its provisions were not brought into force immediately, as the Senate, in giving its approval, had noted that the legislation had flaws that would need to be corrected.

A new consultative process was brought to bear, to draft amending legislation intended to correct the errors noted in the Bill. The amending draft legislation was tabled in June 2007,[FN9] but this legislation became moot when Parliament was prorogued in September 2007. The amending draft legislation was reintroduced in October 2007;[FN10] and after a review process, was approved by Parliament and the Senate, receiving Royal Assent in December 2007.[FN11] While the amending Bill received Royal Assent, its provisions were not brought into force immediately, as it was considered that the stakeholders would require some time to prepare for changes that were considered to be far-reaching. The new legislation, comprised of S.C. 2005 c. 47 as amended and complemented by S.C. 2007, c. 36 (collectively, "new provisions"), was finally brought into force in stages: the first stage on 8 July 2008 and the remainder on 18 September 2009.

While the process of reviewing the legislation was underway, other modifications to the insolvency statutes were introduced, making a true challenge of the task of deciphering which provision was changed, how and when.

One thing that has not changed throughout the process, however, is the fact that one of the main objectives of the modifications, beginning with the mandatory review of 2002, is the necessity of providing better protection to the employees in the event of the insolvency of their employer.

That theme had already been broached when the first round of reform was being contemplated in the early 1990s, as there was then a proposal to create an indemnity fund to pay the claims of employees on the bankruptcy of their employer. That proposal was abandoned in the reform that was implemented on November 30, 1992, largely because a consensus could not be reached as to how the indemnity fund would be financed and by whom.

The objective of better protecting the employees came back on the agenda with the mandatory review of 2002, as the Standing Senate Committee on Banking, Trade and Commerce recommended providing the employees with a first- ranking claim, ahead of secured creditors' security over inventory and accounts receivable, for an amount of up to $2,000.[FN12] The Senate Committee did not go further than that provision, however, and specifically recommended that the claims of pension plans should not be afforded special treatment.[FN13] Despite the recommendations from the Senate Committee, the Parliament saw fit to provide a panoply of new provisions aimed at protecting the employees, recognizing that the employees form a particularly vulnerable group of creditors that are often entirely financially dependent on their employer. The protection measures, in no particular order, are as follows:

- The creation of new legislation, the *Wage Earner Protection Program Act*[FN14] (*WEPPA*) to manage a new program to indemnify employees for their unpaid wages, if their employer becomes bankrupt or in receivership. The program was modified shortly after its creation to also allow a payment in connection with severance or termination pay due when the employer is bankrupt or in receivership.

- Creating a statutory security, ranking in priority to the security held by the secured creditors, to protect

the wage claims of employees[FN15] and certain amounts due to pension funds or in connection with pension plans.[FN16]

• Specifying that an employer undertaking a reorganization process may not assign, disclaim, repudiate or resiliate a collective bargaining agreement or otherwise modify same, except by agreement with the collective bargaining agent.[FN17] Under these provisions, the court may not compel a modification or cancellation of the collective bargaining agreement, but can only order the parties to bargain, and even so only in specific circumstances.

• Providing safeguards to ensure that a restructuring process cannot be used to sell the assets of an employer, thereby defeating the claims of employees or pension plans that would otherwise enjoy a prior ranking statutory security status if the employer were bankrupt.[FN18]

• Requiring the payment of certain claims as a pre-condition to the approval by the Court of a proposal or plan of arrangement.[FN19]

By and large, the measures put in place contemplate a broad range of situations that could arise in an insolvency context, which could affect the employees. These measures represent a large scale improvement over the protection that was previously available for employees, and their implementation has to be lauded. However, the provisions are not perfect, and some difficulties in application have surfaced or have been noted since the measures were drafted. These are discussed in the following sections of this text.

III. — Wage Earner Protection Program Act

The *WEPPA*, implemented on 8 July 2008, creates a program to indemnify the employees whose wages are unpaid because their employer becomes bankrupt or in receivership. Shortly after its implementation, the *WEPPA* was amended,[FN20] to also indemnify employees for severance or termination pay that is due in respect of a loss of employment that results from the bankruptcy or receivership, or that occurred in the 6 months preceding the bankruptcy or receivership.[FN21] While the breadth of the claims was expanded, the maximum indemnity amount was not.

The provisions of the *WEPPA* are meant to co-exist with, and complement the provisions of the *Bankruptcy and Insolvency Act*[FN22] (*BIA*) in dealing with the protection of employees. In this regard, the professional that carries out a mandate under the *BIA*, either as a bankruptcy or receivership, has an important role to play in the context of the *WEPPA*: to notify employees of the existence of the program (WEPP); advise Human Resources and Skills Development Canada[FN23] (HRSDC) of the amounts that may be due to employees; receive and review claims made under the *BIA*; advise HRSDC whether or not a claim has been filed under the *BIA*; and distribute funds to the appropriate party when there is a realization from the current assets of the employer that is bankrupt or in receivership.[FN24]

This last function is particularly important in the context of the WEPP, as the program is intended to act, firstly, as a means to accelerate recovery by the employees. Indeed, one of the employee protection features built into the *BIA* through the new provisions is a statutory security for an amount of up to $2,000 encumbering the current assets of the employer, ranking ahead of the secured creditors' security, for unpaid wages.[FN25] To the extent that the employer has current assets, the claims of the employees should be secured and as such they should not experience a loss. However, some time may pass before a trustee or receiver is able to distribute the proceeds of realization, leaving the employees temporarily without funds at a time when they most need them. The WEPP's

first function is to provide the means to advance funds to the employees, in consideration of a subrogation of the employees' claim against the estate of the employer.[FN26] The right provided HRSDC through subrogation maintains the right to the claim that the employee would have had, in priority and nature, as if the employee had remained the creditor, both in respect of the right to a claim under the *BIA* and the right to seek payment from the directors of a corporate employer, such that the priority afforded by the *BIA* under the new provisions now serves the interests of HRSDC. To the extent that the estate does not have sufficient funds from current asset realizations to reimburse the government for the funds advanced to the employees, and to the extent that the indemnity provided for under the WEPP exceeds the limits of the statutory security under the *BIA*,[FN27] the WEPP acts as an indemnification fund.

The principles behind the WEPP are simple and sound. The program protects employees so that they do not lose wages as a result of the bankruptcy of their employer and so that they are provided with a relatively quick source of funds when they need it most; the program needs to be coordinated with the provisions of the *BIA* where most of the defaulting employer problems are situated; and to be effective the program needs input and attention by insolvency professionals who are the first interveners when a problem surfaces.

Although the principles are simple, problems have been encountered to date in the implementation of the *WEPPA*; more notably the following:

- ensuring that insolvency professionals are remunerated for the tasks they are required to accomplish in the context of the WEPP;
- allocation of responsibility among professionals;
- administrative problems in processing information for use by HRSDC;
- the issue of subrogation of claims of an employee, and who may formulate a claim on behalf of an employee;
- the issue of the scope of the protection afforded by the WEPP; and
- the issue of misalignment of provisions that should be equivalent, between the *WEPPA* and the *BIA*.

These problems are outlined hereunder.

A. — Remuneration of Professionals

As indicated above, the program requires input from and the attention of insolvency professionals in order to function effectively, since the insolvency professionals are the first interveners when a problem surfaces. They constitute an independent, uninterested source of information regarding the position of affected employees.

The *WEPPA* provides for the possibility to pay the remuneration of insolvency professionals for the work they are required to perform in providing information to HRSDC, and in the event there are insufficient assets to pay their fees.[FN28] These provisions were intended to accomplish three objectives: (i) to equitably compensate an insolvency professional for the services provided; (ii) to ensure cooperation of the professionals who are required to do the work, and (iii) to ensure that estates would not be left unadministered solely because a trustee or receiver could not be found to act in a file, if there are insufficient assets to pay the trustee's or receiver's fees. Since access to the program is triggered by a bankruptcy or receivership, it would defeat the purposes if the ac-

cess to the bankruptcy were denied because no trustee would accept to act.

So again, the principles are sound — provide for the payment of the remuneration of the insolvency professional where a shortfall exists, and the program will follow its course smoothly. The problem resides in the implementation. The rules that were put in place to provide for an indemnification in favour of the insolvency professional were intended to limit this indemnification to situations where the funds cannot otherwise be paid from the assets of the estate. They do so very well, since it is next to impossible, with the rules as they are presently written, to obtain an indemnification for the fees and disbursements of the trustee or receiver in the vast majority of cases.

With regards to the fees related specifically to the work performed under *WEPPA*, the regulations[FN29] allow an indemnity only inasmuch as the trustee or receiver incurs a net deficit, i.e. more disbursements than receipts; the trustee does not benefit from a guarantee from a third party creditor of the employer, regardless of the nature of this guarantee — whether asset specific, contingent, partial or unlimited; and the fees relating to the work performed under *WEPPA* are at least 10% of the total fees incurred in the administration.

All conditions have to be met before there can be an entitlement to a payment. The conditions do not take into consideration the fact that some of the estates are summary administrations, where the fees are automatically set as a percentage of receipts,[FN30] such that a net deficit on the statement of receipts and disbursements is impossible. As well, the absence of a guarantee from a third party for either the fees or disbursements may be impossible,[FN31] or so imprudent that it is unlikely to occur.

With regards to the fees relating to the administration of an estate, the regulations[FN32] allow an indemnity only inasmuch as the trustee or receiver incurs a net deficit, i.e. more disbursements than receipts; if no property other than current assets was realized; and if the net current assets realized is a positive amount, i.e. it exceeds the amounts due to "30 day goods" claimants,[FN33] farmers, fishers and aquaculturists[FN34] and deemed trust claims of the Crown,[FN35] but is less than the total entitlement of the employees to the priority afforded by the *BIA* under the new provisions.[FN36]

Again, the conditions have to be met before there can be an entitlement to a payment, and if they are, the payment is limited through a complex formula with little relevance of calculation to the nature of the work performed. The flaws with the conditions are the same as those indicated in respect of the indemnity for the work performed under *WEPPA*. In addition, the conditions of application unfairly disqualify a professional from the indemnity if some amount is realized in connection with fixed assets or intangible property. The variables that affect eligibility are not particularly well defined and as such it is not possible for an insolvency professional to determine with certainty, prior to acceptance of the engagement, whether the conditions will be satisfied if the duties and obligations of the WEPP are fulfilled. The insolvency professional is left with some financial risk.

The conditions of application of the indemnity tend to eliminate the possibility of a payment to the insolvency professional; place the insolvency professional at an unacceptable risk of financial loss; or place an unfair burden on secured creditors who may have security on the fixed assets or intangible property of an employer, to pay the costs of the administration of the estate in their entirety.

The problems raised with the provisions intended to indemnify professionals fairly were identified early, and discussions were initiated with HRSDC with a view to develop an alternative formula that would provide a more appropriate indemnity. Proposals to address the deficiencies have been circulated amongst the Canadian Association of Insolvency and Restructuring Professionals (CAIRP) and HRDSC, with anticipated revisions to the

Regulations at the next round of review.

B. — Allocation of Responsibility Amongst Professionals

This issue is closely related to the issue of the indemnification of professionals, discussed above. The *WEPPA* allocates responsibility to perform certain tasks to insolvency professionals. In order to be certain that someone would be available to perform these tasks, whether or not the employer becomes a bankrupt, the responsibility for the tasks was allocated to both the trustee and the receiver. However, in certain estates, a trustee and a receiver could co-exist, and indeed there could be several receivers, depending on the number of secured creditors and the type of encumbered asset.

In situations where there exists both a trustee and a receiver, or several receivers, the *WEPPA* does not provide a method to allocate responsibility for compliance with the obligations under the statute,[FN37] leaving the possibility of a dispute amongst the professionals as to who should fulfill the obligations. In view of the rules regarding the indemnification of the professional, discussed in the previous section of this text, the professionals are likely to be under some pressure from the secured creditors or guarantors to ensure that the responsibility for compliance is undertaken by someone else.

Ideally, the *WEPPA* should provide a means to allocate the burden for the work performed under *WEPPA* amongst the secured creditors and the estate, if the work is not fully paid for through the indemnity provided to the professional who undertakes to fulfill the obligations.At the same time, however, some process should be put in place to avoid strategies designed solely for the purpose of maximizing the payment by HRSDC under the indemnity for fees, in situations where several professionals have a mandate in an estate, or where a professional assumes several distinct roles in an estate.[FN38] That would also be inequitable.

From my perspective, a fair result would require that the professional who is responsible to realize on the current assets of the employer have the prime responsibility for the performance of the obligations under *WEPPA*, because of the need to coordinate the work under *WEPPA* with the obligations relating to the statutory security given to employees under the *BIA*, which encumbers the current assets only. The fair result would also require that the work required to fulfill the obligations under *WEPPA* be paid by HRSDC without a requirement for the professional to have sustained a deficit, to ensure that the costs of the WEPP are not borne by secured or unsecured creditors. Finally, to ensure access to the bankruptcy system for insolvent employers, an indemnity should be available on a limited basis to cover the fees and expenses of a professional if there are insufficient assets in an estate to cover such proper fees.

C. — Administrative Problems in Processing Information for HRSDC

To run efficiently, the WEPP requires a steady flow of information to ensure that an employee who makes a claim can receive prompt payment. The primary source of that information is the insolvency professional, who is tasked with the obligation to inform HRSDC of, among other items, the amounts due to each of the employees, their personal information and positions with the employer, and whether or not the employee has filed a proof of claim in respect of the amount due.

HRSDC has chosen a web-based entry form to receive the information from the professional fulfilling these obligations. The web-based application does not allow for an automated process to upload the information, but rather requires a manual process to enter each employee record individually. This process is time-consuming and inefficient.[FN39]

In this situation also, the problems were identified early on, and discussions are continuing between CAIRP and HRSDC with a view to improve the efficiency of the data entry system, including the common redundant information as between employees of the same employer. One solution that is being contemplated is modifying the data entry form, the "trustee/receiver information form" (TIF), to ensure that the TIF includes all of the information required of a claim under the *BIA*. The proposed solution would be to allow the trustee or receiver, using the TIF, to file claims in the estate on behalf of employees, subject to the right of each individual employee to subsequently amend the proof of claim. This proposed solution would thus limit the re-entry of information to those exceptional situations where the employee is dissatisfied with the claim that was filed on his or her behalf. It would also eliminate the necessity of the trustee answering on the original TIF that a proof of claim has not been received from an employee, which immediately disqualifies an employee from payment from the WEPP. The disqualification requires a new stream of bureaucratic and administrative steps to resolve.

To date, this proposed solution seems acceptable to CAIRP, to HRSDC, to the Office of the Superintendent of Bankruptcy (OSB) and to Industry Canada, and therefore seems a promising step towards enhancing efficiency. The only word of caution in considering this proposed solution is that from my perspective, the provisions of the *BIA* may require some small amendment in order to accommodate this change. Indeed, the *BIA* already contains a provision that contemplates the filing of claims on behalf of employees.[FN40] This section requires that the claim be filed for the employees collectively and names quite specifically the third parties that are authorized to do so; in its present form, the list of named third parties does not include a trustee or receiver. In view of the existing provisions of the *BIA* that state the requirements for a claim,[FN41] the filing of a claim by a trustee or receiver on behalf of an employee may be improper. Some practitioners believe, however, that a liberal interpretation of the provisions of the *BIA* might allow for the filing of a claim by a trustee, as the trustee could be considered either to be a court-appointed representative, or to be authorized to act on the bankrupt's behalf.

D. — Subrogation of Claims — Who May Formulate a Claim on Behalf of an Employee

This particular issue came to the surface in the case of *Re Ted Leroy Trucking Ltd.*[FN42] In this case, an employee union filed a claim with a receiver, claiming that amounts due to the union in respect of certain of its members constituted salaries, wages or remuneration in virtue of sections 81.3 and 81.4 of the *BIA* and under section 2 of the *WEPPA*. The amounts were not due to the employees individually, but were due to the union in connection with each individual employee and represented charges for union dues, contributions to a health or welfare fund and payments to a third party service provider such as an extended health coverage provider. The union's contention was that the obligation to pay these amounts was contemplated in the collective bargaining agreement and that as a result, these amounts represented for all intents and purposes wages or remuneration due to the employees, for which the relief provided by the *BIA* and *WEPPA* should be available.

The receiver and, on appeal, the secured creditor, asserted that the priority under the *BIA* only applies to amounts due to the employees, and not to amounts due to a third party on their behalf. The Court of Appeal of British Columbia, upholding the decision of the Superior Court, found that benefits payable to a third party can be included in the definition of wages, for the purposes of both the *BIA* and *WEPPA*. It is unclear from the judgments of the lower court and of the Court of Appeal of British Columbia, why the issue of the definition of wages under *WEPPA* was ever considered. While the provisions of *WEPPA* and of the *BIA* co-exist and are somewhat interrelated, they exist independently of one another. It is easy to understand why the receiver and the secured creditor would have an interest in determining the relative claims and priority under the *BIA*. If the claim of the union is found to qualify as a claim under section 81.3 or 81.4 *BIA*, it might displace the claim of a secured creditor.

However, it is far more difficult to understand what would be the interest of the secured creditor in disputing the characterization of the amounts for the purposes of *WEPPA*, since there is no financial implication to the secured creditor arising from the provisions of *WEPPA*.[FN43] HRSDC will be entitled to recover monies from the estate through the subrogation provided for under *WEPPA*, having regard to the otherwise valid claim of the employee. Such subrogation claim entitlement will be determined exclusively under the priority provisions of the *BIA*.

Under *WEPPA*, the determination of whether or not an applicant is eligible for a payment is made by the Minister, based on whether or not the conditions of eligibility have been met.[FN44] As such, the determination of whether or not an amount constitutes wages for purposes of *WEPPA* should only be brought to bear to the extent that a claim was filed and was denied by the Minister. In the case of *Re Ted Leroy Trucking Ltd.*, there is no mention in the judgments that a claim was filed under *WEPPA*, or that the Minister rejected an application for payment, and there is no mention that the Minister intervened in the file.

Still, the Court provided directions regarding the qualification of the claim under both the *BIA* and *WEPPA*, finding essentially that benefits provided for under a collective bargaining agreement or personal employment contract should be liberally interpreted to include such amounts as compensation for services rendered such that the amounts fall within the definition of wages under both the *BIA* and *WEPPA*. Based on this liberal interpretation, such amounts could be part of the compensation entitled to protection under the *BIA* and the *Companies' Creditors Arrangement Act*[FN45] (*CCAA*); and the benefits of the *BIA* and *WEPPA* could extend to amounts that were earned by an employee but that are directed to be paid to a third party, such as a union.

While the judgments are well reasoned and the result seems equitable, they do raise some practical implementation problems, in the context of *WEPPA*, on two levels. First, the judgments deal with the issue of the definition of wages under *WEPPA* and with the fact that the wages of an employee could include amounts due to a third party, but the judgments do not address the issue of subrogation of claims. Under *WEPPA*, the entitlement to a benefit belongs to an employee and is not capable of being assigned.[FN46] If a union formulates a claim under the WEPP for the amounts due to the union on behalf of a claim of the employee, this claim would in effect constitute an assignment of sorts by the employee of his or her entitlement to a benefit under *WEPPA*, which is prohibited.

Second, the judgments do not deal with the allocation of the benefits between the claimants, namely, the amount of the benefit that would be claimed by the employee directly, and the amount of the benefit that would be claimed by the union on behalf of an employee, if the maximum amount of the benefit is reached. Under *WEPPA*, the benefits are subject to a maximum amount for each claimant, and this maximum would need to be allocated as between the employee and the person that claims on behalf of that employee, if the aggregate amount of the claim exceeds the maximum benefit, to avoid a "double-dipping" of the benefits. A similar problem would exist in respect of the maximum amount allowable for the statutory security under the *BIA*.[FN47]

As indicated above, the judgments of the Supreme Court and of the Court of Appeal of British Columbia do not provide any guidance on these practical problems, and we can only hope that future decisions, or a legislative change in the *WEPPA*, will clarify the issue and suggest a solution.

E. — Scope of Protection Afforded by the WEPP

The main objective of the WEPP is to protect the employees in the event of the insolvency of their employer. *WEPPA* provides that benefits can be available to employees when the employer is bankrupt or in receivership,

the employee has lost his or her employment and amounts are due for unpaid wages, remuneration or severance and termination pay. However, there are insolvency situations where employees should be protected, and the legislation offers little or no protection whatsoever. The first such situation is that of the smaller employers who simply close their doors without a formal insolvency proceeding, due to the fact that there are insufficient assets to pay the costs of a proceeding. The employees of these smaller employers may be left without any protection, since the triggering conditions to make a claim under *WEPPA* do not exist.

The second situation relates to employers undergoing a formal restructuring proceeding. Very often in the course of these restructuring proceedings, the employer must curtail the workforce, resulting in job losses that are directly attributable to the insolvency of the employer. However, unless and until the restructuring proceeding fails, the provisions of the *WEPPA* are inapplicable. For example, the provisions of the *WEPPA* will not apply if the restructuring proceedings are successful, however the terminated employees' employment will not be reinstated and they will not be entitled to an indemnity, as the triggering conditions to make a claim under *WEPPA* do not exist.

F. — Misalignment of Provisions between the BIA and WEPPA

This issue is closely related to the problem with the scope of the protection afforded by the WEPP, discussed above. The misalignment of the provisions between the *BIA* and *WEPPA* is particularly relevant in connection with the frame of reference for a claim under each statute when the employer is bankrupt.

Under *WEPPA*, a claim is calculated backwards, in reference to the date of bankruptcy, i.e. the date on which the employer has actually become a bankrupt. The claim that can be submitted is for wages that are unpaid in the six months preceding the bankruptcy, and/or severance and termination pay that is due if the employment terminated on or in the six months before the bankruptcy.[FN48] Under the *BIA*, the claim of an employee is calculated forwards, starting with a date that is six months before the initial bankruptcy event, and ending with the date of bankruptcy.[FN49]

While the difference may seem slight, it can be heavy with consequences in situations where a long restructuring process is taking place. Assuming that in the context of the restructuring process, the employer has had to curtail the workforce, the employees whose employment was terminated may see their right to an indemnity expire. As noted in the previous section above, their rights are nonexistent if the restructuring is successful, but they may have rights to a claim for a benefit under *WEPPA* if the restructuring is unsuccessful and the employer becomes bankrupt. However, since the entitlement to a benefit under *WEPPA* is calculated based on a period of six months before bankruptcy, the employees whose positions were terminated risk losing benefits if the restructuring is protracted and more particularly, if their employment was terminated more than six months prior to the cessation of the restructuring and onset of the bankruptcy proceeding.

This misalignment of provisions has the perverse effect that in some situations where an employer may otherwise have a viable business, it may be in the best interest of former employees to vote against a plan of arrangement or a proposal, or to seek to have the period in which to file a proposal or plan terminated, in order to procure the bankruptcy of their employer, to collect the benefits under *WEPPA*. Considering the objectives of the insolvency legislation, namely to promote restructuring and rehabilitation over liquidation, and of the *WEPPA*, to protect employees in the event of insolvency, the possibility that it may be in the best interest of former employees to cause the bankruptcy of their employer is counterproductive and a nonsense.

G. — WEPPA — Where do we go from here?

Notwithstanding the lengthy discussions of problems associated with the WEPP, the program is worthwhile and accomplishes much in protecting the rights of employees. Certain modifications are advisable; however, these would be improvements on an already good product. CAIRP reports that there are constructive discussions and a high level of collaboration between CAIRP, HRSDC,[FN50] the Canada Revenue Agency and the OSB, in dealing with the problems that surface in the application of the WEPP, and these discussions can only lead to further improvements to the program.

This issue of the scope of the *WEPPA* is addressed in part in legislation tabled in the House of Commons and in the Senate,[FN51] and these bills would seek to extend coverage to situations where an employer has filed a proposal under the *BIA* or a plan of arrangement under the *CCAA*. The change suggested in the draft legislation, as regards the *WEPPA*, would make it applicable in respect of wages owed to employees by employers who have made a proposal under Part III of the *BIA* or a compromise or an arrangement under the *CCAA*.[FN52] The main problem with this draft legislation is that it may be eclipsed by other similar legislation that addresses changes to the insolvency laws, that is scheduled earlier on the Parliamentary agenda and that does not address changes to the *WEPPA*. As well, the two bills are likely insufficient to fully correct the problem, in that the legislation would have to be modified to apply in any instance where a proceeding is initiated under the *BIA* or *CCAA*, not only when a proposal or compromise is filed. This change would likely help as well in correcting the misalignment of provisions referred to above. Of course, a change in the *WEPPA* to ensure that it applies in restructuring situations as well as in the event of bankruptcy or receivership would require some adjustment of the provisions dealing with the information to be provided to the Minister and to the employees, as in restructuring proceedings the insolvency professional does not have the same degree of access and control over the information as in a bankruptcy or receivership.

Given Ottawa's appetite for legislation that affords protection to employees, including the hotly debated issues pertaining to pension priorities, long term disability and health benefit reform, and other proposed employee protection amendments, it is likely that *WEPPA* will again become a focus point in terms of legislative reform in the future.

IV. — Statutory Security under the BIA

The main feature added to the *BIA* to protect employees, and the most widely known, is the statutory super priority created in virtue of sections 81.3 to 81.6. Sections 81.3 and 81.4 refer to the statutory super priority for unpaid wages earned in the period that begins six months before the initial bankruptcy event or receivership and ends with the bankruptcy or receivership. The general rule is that this statutory security is available to protect the unpaid wages of all employees, for an amount of up to $2,000.[FN53] This statutory security encumbers the current assets of the employer, and ranks in priority to the conventional security in favour of secured creditors.[FN54]

Sections 81.5 and 81.6 of the *BIA* refer to the claims relating to pension plans, for unremitted amounts withheld from an employee's salary, contributions payable by the employer to a defined contribution plan, and normal costs, as defined in the *Pension Benefits Standards Regulations, 1985*,[FN55] payable by an employer to a defined benefit plan. The statutory security is available to protect the unpaid amounts due, without a maximum. This statutory security encumbers all assets of the employer, and ranks in priority to the conventional security in favour of secured creditors.[FN56]

To my knowledge, no significant problem has yet surfaced in the courts in respect of the interpretation of these

provisions, except for the issue raised in *Re Ted Leroy Trucking Ltd.*,[FN57] discussed in an earlier section in the context of *WEPPA*. I believe, however, that these provisions are likely to raise practical problems, in connection with the following issues:

- The nature of the statutory security as an "obscure" charge;
- The amount of the security;
- Whether or not a levy is payable to the OSB, in connection with a payment relating to the statutory security;
- The order of priority of charges against an immovable or real property.
- The issue of who bears the economic impact of the statutory charge, if it affects different creditors.

These problems are outlined hereunder.

A. — Nature of the Security

While the charges protect different types of claims, the features of sections 81.3 to 81.6 are, for all intents and purposes, identical. For purposes of the discussion herein, I will address only the situation as it relates to the employee's claims for wages, under sections 81.3 and 81.4, because this is where the problem is likely to be the most acute, although the situation is the same with regards to the claims of pension plans, albeit on a lesser scale, because of the number of claimants involved.

The *BIA* provisions create a statutory security that encumbers assets, to protect certain claims of employees. The security is available to secure the claims both individually and collectively, and there is no need to register or publish the charge for it to exist, nor to take any step to perfect the security; it exists by the mere fact that the statute says it does.

The security is a sort of floating charge over the assets it encumbers, specifically, current assets, in the case of wage claims. The security itself is not created or dependent on the filing of a claim by an individual claimant, but exists as soon as amounts are due to employees. The filing of a claim by an employee merely serves to document the quantum of the claim as it relates to an individual claimant, and to compel the trustee or receiver to make a payment.

By virtue of its mandate, the trustee or receiver is responsible to take possession and realize on the assets encumbered by the security. The trustee or receiver has no choice in the matter; it cannot decide to abandon the assets, for instance, because the statutory security in favour of employees is not published or registered, and in any event, the statutory security does not contemplate enforcement provisions that are independent of the bankruptcy or receivership process. Such enforcement provisions would be difficult or impossible to manage, in view of the fact that the statutory security is intended to apply only when the employer is bankrupt or in receivership, and that it exists collectively to protect the claims of each employee, individually. By virtue of sections 81.3(5) and 81.4(5) of the *BIA*, the trustee or receiver is compelled to distribute the proceeds of realization to the individual claimants, as these sections attribute a personal liability to the trustee or receiver if it fails to do so.

We can see from the above that the security created in favour of employees by the *BIA* is an "obscure" security. It exists without publication, registration or perfection, and while the claimants can be identified, the claimants

and claim amounts cannot be known with absolute certainty, since under the *BIA* it is the responsibility of the creditor to prove its claim.[FN58]

While the *BIA* provides that it is the creditor's responsibility to prove a claim, the *BIA* does not set a deadline to do so, except in the context of the claims bar process described in section 149 of the *BIA*. This process is available to a trustee in bankruptcy to create a claims bar date, but does not apply to a receiver. In view of the fact that there is no set deadline to file a claim, there is some degree of risk for a trustee or receiver associated with the fact that the security is obscure. If the trustee or receiver takes possession and realizes on the assets, distributes proceeds to the employees that have filed claims, and then distributes the remainder of the proceeds to the secured creditors or ordinary unsecured creditors, the trustee or receiver could be personally liable if, subsequently, another employee files a claim for unpaid wages. We can only hope that a demonstration that good faith efforts and prudence were applied would serve as a due diligence defence to excuse the trustee or receiver from personal liability.

The situation would be the same if the assets are insufficient to pay all of the claims of the employees, and an employee files a claim after a distribution has been made to the other employees. The trustee or receiver could be personally liable because of a delay that is not caused by the trustee or receiver, but by the claimant himself/herself. In view of the potential risk for the insolvency professional, it would seem prudent to ensure that no distribution is made to employees or to others, until a claims bar process has been put in place. As indicated above, the *BIA* allows for a claim bar process of sorts under section 149, for a trustee that intends to make a distribution, although this claim bar process may not be perfect, since it presupposes that all claimants are known and can be contacted by mail. Since the super priority is an obscure charge, a claims bar process should involve some notification in the media, ideally. And as noted above, the claim bar process that exists under the *BIA* is not available to a receiver, although if the receiver is appointed by the Court under *BIA* section 243, it is possible that the Court could have discretion to create a claims bar process.

From an insolvency professional's perspective, I would prefer that the legislation be amended to provide that the liability of a trustee or receiver is limited to the funds on hand, such that the trustee or receiver could not be liable towards an employee that has filed his or her claim late. However, I can understand that Parliament could be reticent to make such a provision, to avoid a situation where the funds are distributed expeditiously to benefit a secured creditor at the expense of employees. Perhaps some middle ground can be found, where a trustee or receiver has to wait a reasonable period of time after its appointment before proceeding to any distribution, failing which its personal liability is engaged, and limit the liability subsequently to the funds on hand.

B. — The Amount of the Security

Again, as in the previous section, I will focus my comments on the provisions of sections 81.3 and 81.4 of the *BIA*, dealing with the claims of employees, although the comments apply equally to the claims of pension plans under *BIA* sections 81.5 and 81.6. I indicated in the previous section that the trustee or receiver is responsible to take possession of the assets encumbered by the statutory security, and must distribute the proceeds of realization firstly to the employees, as it will incur personal liability to the employees if it fails to do so.

We know from the statute what the maximum amount of the security is: It is the aggregate of the amounts due to the employees individually, provided that each individual amount relates to the period for which the security is granted, specifically, the period starting six months before the initial bankruptcy event or receivership and ending with the bankruptcy or receivership; and does not exceed $2,000 per employee.[FN59]

What we don't know is the actual amount of the security. We know from section 81.3(5) and section 81.4(5) of the *BIA* that if a trustee or receiver takes possession and disposes of the assets, its personal liability is calculated as the "amount realized on the disposition of the current assets". The statute is painfully silent on the meaning of this sentence, and unfortunately the French version of the statute, which refers to the "produit de la disposition", does not provide any additional guidance.

It is impossible to determine with certainty, from the language of the statute, whether Parliament intended to make the trustee or receiver responsible for the gross amount realized, or for the net amount realized, and in this latter case, whether the net amount realized should take into consideration the remuneration of the trustee or receiver to realize upon the assets. Since the statutory security does not provide for an enforcement mechanism outside of the payment of the claim by the receiver or trustee, logic would dictate, since slavery was abolished in Canada in the 1830s, that the security can only attach to the net realized value, after all reasonable costs incurred to convert the assets into cash.

C. — Levy Payable to the OSB

Section 147 of the *BIA* requires that a levy be paid to the OSB, on all payments, except the costs referred to in *BIA* section 70(2), made by a trustee by way of dividend or otherwise, on account of the creditors' claims. The issue of whether or not a levy applies to a payment to a secured creditor has been a topic of contention for some time, resulting in a long list of decisions by the courts.

In an attempt to cut short the discussions and arrive at a uniform treatment, the OSB issued a directive dealing with payments to secured creditors and the levy, namely Directive No. 10 issued 19 December 1997. This directive was determined by the Court to be *ultra vires*,[FN60] and as a result the directive was withdrawn and reissued as Directive No. 10R on 22 May 2009.

Directive No. 10R is quite straightforward in its provisions, but does not provide the clarity required to ensure disputes no longer arise, regarding whether or not a levy is payable on a payment to a secured creditor. In short, Directive No. 10R provides that a levy is payable on all payments made by a trustee, including payments to secured creditors, except where the trustee acts as the agent of the secured creditor, or where the trustee proceeds to redeem the security within the meaning of section 128 of the *BIA*.

In fact, Directive No. 10R merely repeats what the *BIA* dictates at section 147, allowing for the exceptions that were developed through jurisprudence, in a very generic manner. A long list of decisions has wrestled with the concepts of determining the nature of a redemption, whether or not a redemption had taken place based on factual sets of circumstances, or whether or not a professional acted in its quality as trustee or as an agent in performing certain tasks. These issues are not discussed in the directive.

The issue is relevant, because the insolvency professionals are now left with the task of characterizing the payment made to employees under section 81.3 of the *BIA*. In this particular respect, I purposefully did not mention *BIA* section 81.4, since the levy only applies to payments made by a trustee, not a receiver. As such, if it is determined that a payment made by a trustee on account of the employees' claims attracts a levy, then we are faced with the strange situation that the outcome for the employees might be different, in a given file, depending on whether the insolvency professional that issues the payment is a trustee or a receiver.

From the OSB's preliminary analysis, a payment to the employees of their secured claim under section 81.3 of the *BIA* would always attract a levy. The OSB's preliminary analysis is premised upon the fact that the employ-

ees have no independent enforcement mechanisms in respect of their security, i.e. an *in rem* right, and that as a result they are compelled to rely on the bankruptcy process, by delivering a proof of claim to the trustee and obtaining payment through the normal course distribution of assets through the administration of the estate. The OSB considers that this process does not lead to a redemption of the employees' security, which would exempt the payment from the levy, but rather to a payment by the trustee on account of the creditors' claims, which does attract a levy. The OSB considers that a payment by a trustee could not be considered a redemption, since a trustee should only redeem security where this redemption procures an advantage for the estate, and this advantage is not readily apparent where the trustee is obliged to make payments because of the statute itself, and the secured creditor cannot force the sale of the property thus removing the equity of redemption in the said property from the control of the estate.

From my perspective, I believe that because of the manner in which the statute is constructed, the payment of the claim by the trustee is indeed a redemption of the security, and that as a result a levy does not apply.

There is no question that the nature of the right that exists in favour of employees is that of security. The language of the statute, at section 81.3(1), is clear in this regard. It is true that there is no independent enforcement mechanism allowing the beneficiaries of the security to seize the collateral and bring it to a sale. That does not mean, however, that the employees are devoid of any enforcement mechanism; it only reflects the fact that this security was intended by Parliament to apply solely in the event of bankruptcy or receivership, and that it would be impossible to manage enforcement provisions in respect of security available on a collective basis to protect the claims of employees individually.

The employees indeed have an enforcement mechanism built into the statute, which is the personal liability of the trustee or receiver. The statute creates the security in favour of employees, which as we have seen in the previous section exists independently of whether or not the employees have filed a claim — if an amount is due, the security attaches to the current assets, even if the employee has not filed his or her claim. The personal liability provision allows a means for the security to attach to replacement property and to prevent conversion (i.e. a payment to a third party without regard to the employee's secured claim). Then the statute provides a means for the employee to realize on his or her security, by compelling payment when a proof of claim is filed. In the context of sections 81.3 and 81.4 of the *BIA*, the proof of claim is not only a means to document or quantify the claim, but it is also a means to force payment, since payment of the claim is the only way for the professional to discharge its personal liability.

From my perspective, the process described above represents an effective enforcement process, in which Parliament has replaced the right to obtain possession of the assets for purposes of realization, the *in rem* right, by a right to claim replacement property supplemented by a process to prevent conversion, i.e. the personal liability aspect of *BIA* s. 81.3.

Furthermore, it cannot be said that the payment is not a redemption, since the fact that the trustee performs its functions under the *BIA* by taking possession and realizing upon the current assets will necessarily result in an advantage for the estate, as is explained hereunder.

Section 81.3(1) of the *BIA* states that the claims of the employees are secured by security over all of the current assets of the employer. Section 81.3(5) of the *BIA* defines that when a trustee disposes of the current assets, he is personally liable to the extent of the amount realized. As we have discussed in an earlier section above, the concept of the amount realized can logically only refer to the net amount realized, after the costs of realization.

It would therefore appear that the construction of the statute itself provides a means to reduce the security below its original amount (i.e. all of the current assets) to an amount no greater than its net realized value. Meanwhile, we know that a trustee has an obligation under the statute to take possession of the assets and insure them, forthwith upon its appointment,[FN61] although it is not required to realize upon the assets if there is no equity therein. As a result, the trustee is required to incur costs immediately upon its appointment, which may not be recoverable if the assets are subsequently abandoned. In view of the construction of section 81.3, these costs become automatically recoverable if the trustee disposes of the assets, since they will form part of the costs of realization associated with the property. Consequently, the construction of section 81.3 itself provides a net benefit to the estate, by creating a recovery of sunk costs, if the trustee proceeds to realize upon the assets thus redeeming the security.

In view of the above, I consider that the construction of the statute itself provides an enforcement mechanism and a benefit from the redemption of assets, such that when the trustee makes the unilateral decision to redeem, by realizing on the assets rather than abandoning them, all conditions required in the jurisprudence to except a payment from the application of a levy have been met.

I am not aware of any situation where the problem has surfaced yet; and I believe that the OSB has not yet completed its analysis of the issue, since it has only sent a draft position paper to CAIRP for comments and has not yet issued a formal position paper to practitioners. We can hope that the issue is determined soon, either by the issuance of a satisfactory position paper from the OSB or by the courts, as this issue is likely to affect a large population of creditors. As mentioned above, this issue is not limited to the claims of employees, but would also affect the claims of pension plans under section 81.5 of the *BIA*.

D. — Order of Priority Against an Immovable or Real Property

This issue affects only the claims of pension plans under section 81.5 of the *BIA*,[FN62] and results from contradicting provisions in various statutes regarding the priority of claims. Section 81.5(2) of the *BIA* specifies that the security created in virtue of section 81.5(1) *BIA* ranks immediately after the claims of the unpaid vendors under sections 81.1 and 81.2 *BIA*, the deemed trust for payroll source deductions under section 67(3) *BIA* and the claims of employees under section 81.3 and 81.4 *BIA*. In view of this section, the secured claim of the pension plan ranks after the deemed trust claim of the Crown (among others) and before conventional security of a secured creditor.

However, in virtue of sections 227(4.1) and 227(4.2) of the *Income Tax Act*[FN63] and section 2201 of the *Income Tax Regulations*,[FN64] a mortgage that encumbers an immovable (real) property, if the mortgage was granted before the deemed trust came to exist, would have precedence over the deemed trust. It therefore appears, by looking at these provisions together, that with regards to an immovable property, the deemed trust claim of the Crown ranks in priority to the security in favour of a pension plan, which in turn ranks ahead of a mortgage, which in turn ranks ahead of the deemed trust claim of the Crown. This is a nonsensical situation.

E. — Economic Impact of the Statutory Charge when there are Several Secured Creditors

Parliament, in creating the statutory charges to protect employees and pension plans, has not created any "marshalling" scheme. This exacerbates a problem that already existed because of the statutory deemed trust for payroll source deductions. In effect, the problem stems from the fact that the statutory deemed trust (which under the *BIA* ranks ahead of the employees' and pension plans' security under sections 81.3 to 81.6) charges any asset of the employer, while the employee's statutory security charges any current asset, and the pension plan

charges any asset of the employer.

In a situation where different secured creditors have security over different assets, the question of which creditor bears the burden of the statutory charges and deemed trust is an important one. The new provisions provide a right for the affected secured creditor to claim as a preferred creditor in the estate, to the extent that it is prejudiced by the statutory security in favour of the employees or the pension plans. However, this preferred claim may be insufficient protection if the assets are all encumbered, and it might be preferable from the secured creditors' perspective to have a clear methodology to allocate the burden, in cases where the value of the assets is insufficient to cover all of the statutory and non statutory charges and deemed trusts.

V. — Collective Bargaining Agreements and Wage Claims

One of the features of protection built into the legislation was the fact that a collective bargaining agreement cannot be assigned, resiliated, repudiated, disclaimed or otherwise modified unilaterally in the context of a restructuring process. Both the *BIA* and *CCAA* contain provisions prohibiting modifications to collective bargaining agreements. The only influence that the court overseeing the proceeding may have is to authorize the debtor to serve a notice to bargain, and that authorization may only be granted on stringent conditions.

It appears that Parliament wanted to protect unconditionally the collective bargaining agreement, by making it sacrosanct. Problems rapidly surfaced, however, in determining what forms or does not form part of the collective bargaining agreement, and what is meant exactly by the concept that the collective bargaining agreement cannot be modified. More specifically, a collective bargaining agreement tends to manage all aspects of the relationship between an employer and a group of employees. The collective bargaining agreement will address not only the salary of the work force, but may also address seniority lists and rights of recall, fringe benefits, payments to former employees after they retire, entitlement to early retirement, in fact anything that the parties see fit to address that relates to the employer-employee relationship. Does the fact that a collective bargaining agreement cannot be modified mean that all amounts that are ever referred to therein must be paid unconditionally? If the collective bargaining agreement contemplates the payment of retirement benefits to former employees who are now retirees, must these payments continue unaffected?

Some of these issues are not easily resolved, as the easy path of considering the collective bargaining agreement as unconditionally cast in concrete could lead to the demise of the employer, or from a labour perspective, a situation where the operation is a success even though the patient is deceased.

To resolve this problem, the courts started modulating the stance regarding the sanctity of the provisions of the collective bargaining agreement. The efforts of the courts to allow flexibility to ensure that the restructuring process continues while abiding by the requirement to leave the collective bargaining agreement unaffected has led to decisions that are interesting from a practical view point, but that are difficult to reconcile.

Some examples follow.

> • In February 2010, the Superior Court of Québec made an initial order in the matter of the proposed plan of arrangement of White Birch Paper Holding Company and its affiliates.[FN65] In the context of the initial order, the Court authorized the debtor to suspend the payment of the special payments due in connection with various pension plans, notwithstanding the fact that the payment of pension contributions was provided for in the collective bargaining agreement for those employees that are unionized. Relying on the findings of the Court in proceedings under the *CCAA* in respect of AbitibiBowater Inc.,[FN66] the

Court decided that the special payments were "pre-filing" obligations for which payment could be suspended.

• In the AbitibiBowater file, the Court had occasion to consider the impact of an obligation contained in the collective bargaining agreement, which clearly related to work performed before the initial order was granted. In a judgment rendered in May 2009,[FN67] the Court had to decide whether the debtor company could suspend a right to take early retirement, as provided for in a collective bargaining agreement. The initial order had been made in mid- April 2009, and the debtor Company announced to its employees that the early retirement program would not be available after May 1, 2009. The employees' union requested that the Court review and reverse the Company's decision in this regard, since certain employees would be eligible to take early retirement and wanted to avail themselves of this possibility. The Court determined that the Company's decision to terminate the early retirement program was illegal. In its judgment, the Court reiterates the principle that while the collective agreement is unchanged, this does not require a payment for the obligations in connection with services rendered before the initial order, but rather defines the basis of the remuneration for the services rendered after the initial order, which must respect the terms of the collective bargaining agreement integrally. In short, the Court declares that the decision of the Company to suspend the early retirement program is illegal, and bases its decision in this regard on the provisions of section 11.3 of the *CCAA* (currently section 11.01), stating that since the employees worked a few days after the initial order and that the terms of their employment were premised upon the collective bargaining agreement that must remain unchanged, then the right to an early retirement was part of their compensation for the few days worked after the initial order, such that the entitlement to the early retirement is part of the post-proceeding compensation for services rendered.

• Turning again to the White Birch file, the Court also had occasion, in a judgment rendered in June 2010, [FN68] to consider the obligations contained in the collective bargaining agreement, also in the context of the benefits due in connection with an early retirement program. This case is different from the decision referred to above in respect of AbitibiBowater, because the White Birch file is governed by the new rules that came in effect in September 2009 (while section 33 of the *CCAA* was not in force and does not apply to the proceedings of AbitibiBowater), and because the right that was being considered by the Court was not whether an early retirement program should apply, but rather whether the amounts due to former employees, now retired, under an existing early retirement program could be suspended. The employees' union contended that in view of the text of section 33 of the *CCAA*, the provisions of the collective bargaining agreement had to be applied integrally, which, for the union, meant that the benefits contemplated in the collective bargaining agreement, payable to former employees that are no longer providing services to the debtor company, should continue integrally. In a detailed decision, the Court found that section 33 of the *CCAA* is substantially a codification of existing jurisprudence rather than "new law" and that, if the collective bargaining agreement must remain unchanged, this does not mean that it escapes completely the effect of the restructuring under the *CCAA*. The Court found that the collective bargaining agreement could protect the employees currently working for the debtor company, but not the former employees who are no longer providing services.

It is difficult to distinguish the reasons why the right to benefit from an early retirement program a few days after the initial order would be a post-proceeding obligation, while the right to obtain an on-going payment of the amounts required to fund a pension deficit, i.e. the past service contributions, is a pre-proceeding claim. Intuitively, it would appear that the right to a pension, on the terms provided for in the collective bargaining agreement, is a condition of the continued employment, such that even though the obligation is described as a "past

service cost", it is indeed part of the compensation for services rendered post-proceeding.

While the distinction is difficult to comprehend, we have to admit that the result is attractive from the perspective of the restructuring debtor enterprise, particularly in a situation where the past service costs would be so significant as to put in doubt the viability of the employer.

The decisions referred to above appear to suggest that the collective bargaining agreement must remain unchanged. However, inasmuch as the collective bargaining agreement seeks to address amounts due for services rendered in the past, the right to enforce payment may be suspended and the provisions of the collective bargaining agreement will only benefit employees that are currently employed and providing services to the debtor company. These findings seem consistent with the prior jurisprudence that evolved in Québec.

In the judgment rendered in June 2010 in *re White Birch*,[FN69] the Court mentions that in interpreting section 33 of the *CCAA*, one cannot give such rigidity to the collective bargaining agreement as to give the union a quasi-complete control over the restructuring process, as this would deprive the *CCAA* of its flexibility and efficiency.

VI. — Conditions of Approval of a Plan or Proposal

The portion of the revisions brought into force in September 2009 builds on a provision that existed in the *BIA* regarding the payment of the claims of the employees in the context of a reorganization process. The *BIA* already provided that a proposal must provide for the payment of the employees' claim, to the extent that these claims could be preferred in a bankruptcy, and of all amounts due to the employees for services rendered in the period subsequent to the inception of the restructuring process, immediately after the approval of the proposal by the court and, further, that the court be satisfied that the employer can and will make these payments.[FN70] An equivalent provision was introduced in the *CCAA*.[FN71]

As well, a similar provision was introduced in both the *BIA* and *CCAA*, in connection with claims relating to pension plans, although with slight differences, in that the provision relating to pension plan claims does not require an immediate payment, and allows some leeway for an agreement to pay less than the full amount due, by agreement between the employer and the pension plan, if the relevant pension regulator has approved the agreement.[FN72]

The provisions are simple enough, but present a problem from a practical point of view, on two levels: First, with regard to the requirements to satisfy the court that the employer can and will make the payments in a situation where the payments are not contemplated to be made immediately. It is difficult to assess how demanding the standards will be to convince the court of an ability to fulfill this requirement, short of making the payment. Second, with regard to the need for an immediate payment of employee claims. Typically, a large portion of employees' claims is comprised of amounts due for annual vacations or other deferred benefits, which are usually paid on an on-going basis, as and when they become due. A necessity to pay all of these amounts immediately after the approval by the court of the proposal or plan could have a large impact on the employer's cash flow, as payment may be required prior to the availability of exit financing.

VII. — Proposed New Legislation

While great strides were made to protect the claims of employees in insolvency proceedings in the modifications implemented in July 2008 and September 2009, some stakeholders believe much is still required. The difficult

economic conditions that prevailed since 2007 have resulted in insolvency proceedings of large corporate employers, thus affecting a very large number of employees. In the past year alone, there have been five bills [FN73] tabled, three in the House of Commons and two in the Senate, all dealing with a proposed enhancement of the protection afforded to employees in the event of the insolvency of their employer.

The bills cover topics such as:

• Pension plan liabilities[FN74] — to provide a measure of protection for special payments due in respect of pension plans, and/or for the entire pension deficit, if the employer becomes insolvent or bankrupt while the plan is in a deficit position.

• Severance and termination pay[FN75] — to provide a super priority statutory security to protect all severance and termination pay claims of employees who are terminated in a context of a bankruptcy or receivership, and to compel payment of these claims as a condition for the approval of a proposal or plan of arrangement.

• Directors' liability[FN76] — to provide a streamlined process to assert a claim against directors, for companies incorporated under the *Canada Business Corporations Act*.[FN77]

• *WEPPA*[FN78] — to extend the protection of the WEPP to situations where the employer has filed a proposal or a plan of arrangement.

• Disability and health plan liabilities[FN79] — to provide a measure of protection for employees that are beneficiaries of a long term disability plan or a health plan provided by their employer.

• Employment insurance — to eliminate the "claw back" provisions of the employment insurance legislation in situations where employees receive a distribution by way of dividend on account of their claim.

I will not discuss the contents of the bills and my thoughts regarding the various provisions; an analysis of the various proposed changes could in itself form the basis for a lengthy paper. Both CAIRP and the Insolvency Institute of Canada (IIC) recently submitted position papers in connection with these bills that provide a good perspective of the proposed new provisions, from the point of view of the practitioners who are involved in the insolvency process. Both organisations' position papers express concern over the impact that some of the proposed changes could have on the availability of credit. It is felt that some of the proposed changes intended to enhance the protection available to employees in the event of insolvency could result in a severe contraction of credit for all enterprises, which could affect the economy as a whole, and result in the insolvency of enterprises that are otherwise capable of surviving. The contraction of credit and resulting possibility of forcing enterprises that are otherwise surviving into an insolvency proceeding could lead to a loss of employment, which would be counterproductive to the stated objective of protecting the employees.[FN80]

VIII. — Conclusion

The previous sections analyzed the various changes made to the insolvency legislation through the new provisions to protect employees in the event of the insolvency of their employer, in particular with regards to the practical problems that have been encountered to date in the implementation of these new provisions. While some problems have been encountered, they do not appear to represent fundamental flaws; the legislation seems to accomplish its stated objective, and the professionals charged with administering the provisions are working

through the kinks. It is apparent that the government is focusing on the issue of protection of employees' rights, even more so considering the publicity surrounding some of the recent large insolvency proceedings and how the employees' pension, long term disability and other health benefits may be affected. The public attention raised by the plight of the employees affected by these large insolvency files ensures that the issue of employee rights will remain a focus point for the government, and this is reflected by the fact that there are currently five bills emanating from the House Commons or the Senate dealing with the issue.

It is very easy to be sympathetic to the plight of these employees. In general, employees represent a vulnerable group of creditors who are entirely dependent on their employer for their livelihood, and who don't have an independent way to monitor and control their loss exposure. The employees should not have to suffer a loss of their acquired benefits, in addition to losing their source of future income. However, in attempting to protect the employees' rights, it is important that we do not compound the problem by affecting the economy in a way such that the resulting effect might be an overall loss of employment in Canada.

It is important to keep sight of the fact that the large insolvency files that served to bring the problem to the public view may be an unusual set of circumstances caused by particularly difficult economic conditions, and that the problems may not be as deep as is currently perceived, but that the economic crisis may have blown the problem completely out of proportions. We have to ensure that an overblown problem does not trigger a set of solutions that goes overboard and has unintended, unfavourable consequences on the economy.

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FN2. *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, S.C. 2005, c. 47 as amended and complemented by *An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005*, S.C. 2007, c. 36.

FN3. *An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act and the Income Tax Act*, S.C. 1997, c. 12, ss. 114 and 126.

FN4. Standing Senate Committee on Banking Trade and Commerce, *Debtors and Creditors Sharing the Burden: A review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act*, November 2003 [*Debtors and Creditors Sharing the Burden*].

FN5. Bill C-55, *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, 1st Sess., 38th Parl., 2005.

FN6. See e.g. the submissions presented by the Canadian Association of Insolvency and Restructuring Professionals ("CAIRP") in October and November 2005, online: CAIRP <www.cairp.ca/publications/submissions-to-government/index.php>.

FN7. The 38th Parliament was led by a minority government and at the time of this draft legislation, Bill C-55,

there were widespread rumors that the government would soon be defeated. The Bill was considered to contain important social policy changes that would resonate with the electorate. However, the Bill did not have the desired impact in the context of the ensuing election because of the fact that all parties supported it in Parliament.

FN8. Bill C-55 received Royal assent on 25 November 2005, to become S.C. 2005, c. 47.

FN9. Bill C-62, *An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005*, 1st. Sess., 39th Parl., 2007.

FN10. Bill C-12, *An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005*, 2nd Sess., 39th Parl., 2007.

FN11. Bill C-12 received Royal assent on 14 December 2007 to become S.C. 2007, c. 36.

FN12. *Debtors and Creditors Sharing the Burden*, *supra*, note 3, at recommendation no. 20.

FN13. *Ibid.*, at recommendation no. 21.

FN14. *Wage Earner Protection Program Act*, S.C. 2005, c. 47, s. 1 [*WEPPA*].

FN15. *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, ss. 81.3 and 81.4 [*BIA*].

FN16. *Ibid.*, ss. 81-5 and 81.6.

FN17. *Ibid.*, ss. 65.11(10), 65.12 and 84.1; and *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, ss. 11.3, 32(9) and 33 [*CCAA*].

FN18. *BIA*, *supra*, note 14, s. 65.13(8); and *CCAA*, *supra*, note 16, s. 36(7).

FN19. *BIA*, *supra*, note 14, ss. 60(1.3), 60(1.5) and 60(1.6); *CCAA*, *supra*, note 16, ss. 6(5) to 6(7).

FN20. *Budget Implementation Act, 2009*, S.C. 2009, c. 2.

FN21. *WEPPA*, *supra*, note 13, s. 2(1)(b).

FN22. *BIA*, *supra*, note 14.

FN23. Section 3 of the *WEPPA* indicates that the WEPP is the responsibility of a Minister designated by the Governor in Council. The *Wage Earner Protection Program Regulations* SOR/2008-222 [WEPPR] disclose that the Minister of Labour was designated as the Minister responsible for the WEPP. The program is delivered by Service Canada, an organ of HRSDC, on behalf of the Labour Program, online: HRSDC >www.hrsdc.gc.ca/eng/corporate/about us/index.shtml> and Service Canada <www.servicecanada.gc.ca/eng/sc/wepp/index.shtml>.

FN24. *WEPPA*, *supra*, note 13, s. 21; *BIA*, *supra*, note 14, ss. 81.3 and 81.4.

FN25. *BIA*, *ibid.* (It should be noted that the statutory security could exceed $2,000, if the employee is a travel-

ling salesperson who has incurred expenses on behalf of his or her employer, and that the wage claims of certain categories of employees may not benefit from the statutory security, however this discussion is not relevant for the purposes of this article).

FN26. *WEPPA*, *supra*, note 13, s. 36.

FN27. For example, if the claim exceeds the $2,000 limit or if the claim relates to severance or termination, which are not defined as wages for purpose of the *BIA*.

FN28. *WEPPA*, *supra*, note 13, s. 22; and *WEPPR*, *supra*, note 22, ss. 18 and 19.

FN29. *WEPPR*, *ibid.*, s. 18.

FN30. *Bankruptcy and Insolvency General Rules*, C.R.C., c. 36, s. 128.

FN31. For example, section 45(2) of the *BIA*, *supra* note 14 provides for a statutory indemnification in favour of the trustee for the costs incurred by the trustee (but likely not its fees), in case of an application for a bankruptcy order.

FN32. *WEPPR*, *supra*, note 22, s. 19.

FN33. *BIA*, *supra*, note 14, s. 81.1.

FN34. *Ibid.*, s. 81.2.

FN35. The amounts referred to in section 67(3) of the *BIA*, *ibid.*, which would include the deemed trusts created in virtue of section 227(4.1) of the *Income Tax Act*, R.S.C. 1985, (5th Supp.), c. 1; section 86 of the *Employment Insurance Act*, S.C. 1996, c. 23; section 23 of the *Canada Pension Plan*, R.S.C. 1985, c. C-8; and section 20 of the *Act respecting the ministère du revenu*, R.S.Q., c. M-31.

FN36. *BIA*, *supra*, note 14, ss. 81.3 and 81.4.

FN37. *WEPPA*, *supra*, note 13, s. 21.

FN38. This could occur where the responsibility for fulfilling the obligations under the *WEPPA* is strategically allocated among the professionals based on the availability of an indemnity rather than based on resources or ease of access to the information required to fulfill the obligations.

FN39. In the early part of the WEPP, the web-based entry process did not allow for amendments of previous entries, but rather required a complete re-entry of all information pertaining to the employee's record, making an inefficient process all the more frustrating. This problem has since been corrected.

FN40. *BIA*, *supra*, note 14, s. 126(2).

FN41. Section 124(3) of the *BIA*, *ibid.*, requires that a claim be made by the creditor himself or by a person authorized by the creditor.

FN42. *Re Ted Leroy Trucking Ltd.*, 2010 BCCA 223 (B.C. C.A.) [*Ted Leroy Trucking* (BCCA)], and *Re Ted Leroy Trucking Ltd.*, 2009 BCSC 41, 52 C.B.R. (5th) 225 (B.C. S.C.); affirmed 2010 CarswellBC 1109 (B.C.

C.A.) [*Ted Leroy Trucking* (BCSC)].

FN43. Of course, other than the funding of the administrative compliance by an insolvency professional. However, the issue of compliance (and thus funding for this compliance) is not affected by the characterization of the payment as wages or not.

FN44. *WEPPA*, *supra*, note 13, s. 9.

FN45. *CCAA*, *supra*, note 16.

FN46. *WEPPA*, *supra*, note 13, s. 37.

FN47. Conceivably, the problem could be resolved by the employee including all the entitlements payable to a third party in his or her own claim, and reimbursing the amounts recovered to the third party, however this solution is not very practical, as the amounts due on behalf of the employees collectively to a third party may be difficult to apportion on an employee by employee basis, and because of the difficulty for the third party in managing the collection of the amounts received from each employee.

FN48. *WEPPA*, *supra*, note 13, s. 2.

FN49. *BIA*, *supra*, note 14, s. 81.3.

FN50. HRSDC, including Service Canada.

FN51. Bill C-476, *An Act to amend the Bankruptcy and Insolvency Act and other Acts (unfunded pension liabilities)*, 3rd Sess., 40th Parl. 2010; and Bill S-214, *An Act to amend the Bankruptcy and Insolvency Act and other Acts (unfunded pension liabilities)*, 3rd Sess., 40th Parl. 2010.

FN52. In my view, the change as suggested in Bills C-476 and S-214, *supra* note 51, as regards *WEPPA*, is insufficient as other sections of *WEPPA* would also need to be adjusted to accommodate the concept of a payment to employees when there is a loss of employment as a result of a restructuring proceeding under the *BIA* or *CCAA*. The other areas that would require consequential changes include, for instance, clarifying the responsibility of the debtor, trustee, receiver or monitor for providing information to HRSDC in pursuance of the legislation, and adjusting the language of *WEPPA*, *supra* note 13, ss. 5 and 7(2) to remove the limitations imposed regarding the occurrence of a bankruptcy or receivership. Similar changes would also be required to the *WEPPR*, *supra*, note 22.

FN53. An additional amount of up to $1,000 is available for expenses of a travelling salesperson incurred in the course of the employer's business. The statutory security protects the wage claims of employees other than officers and directors. As well, an employee who did not deal with the employer at arm's length may not benefit from the statutory security, unless the trustee or receiver, as the case may be, is satisfied that the conditions of employment would have been the same if the parties had dealt at arm's length.

FN54. The statutory security is subject only to the rights of unpaid vendors under ss. 81.1 and 81.2 of the *BIA*, *supra*, note 14, and the deemed trust claims of the Crown for payroll source withholdings, as described in s. 67(3) of the *BIA*.

FN55. SOR/87-19, the regulations to the *Pension Benefits Standards Act*, R.S.C. 1985, (2nd Supp.), c. 32.

FN56. The statutory security is subject only to the rights of unpaid vendors under ss. 81.1 and 81.2 of the *BIA*, *supra* note 14; the deemed trust claims of the Crown for payroll source withholdings, as described in s. 67(3) of the *BIA*; and the statutory security in favour of employees, under ss. 81.3 and 81.4 of the *BIA*.

FN57. *Re Ted Leroy Trucking Ltd.*, *supra*, note 41.

FN58. *BIA*, *supra*, note 14, s. 124.

FN59. See the comments at note 52 above.

FN60. *Climenhaga v. Alberta (Superintendent of Bankruptcy)* (2008), 2008 ABQB 340, *(*sub nom. *Re Cutting Edge Foods Inc. (Bankrupt))* 456 A.R. 40, [2009] 8 W.W.R. 113 (Alta. Q.B.).

FN61. *BIA*, *supra*, note 14, ss. 16(3) and 24.

FN62. From my perspective, the problem also exists in respect of section 81.6 of the *BIA*, *ibid.*, although it is less obvious, since *BIA* s. 81.6(2), addressing the ranking of the security, does not refer to *BIA* s. 67(3).

FN63. *Income Tax Act*, *supra*, note 34.

FN64. *Income Tax Regulations*, C.R.C., c. 945.

FN65. *Re White Birch Paper Holding Co.*, 2010 QCCS 764, 2010 CarswellQue 1780 (Que. Bktcy.) [*White Birch* (Mar. 2010)].

FN66. *Re AbitibiBowater inc.*, 2009 QCCS 2028, [2009] R.J.Q. 1415, 57 C.B.R. (5th) 285 (Que. S.C.).

FN67. *Re AbitibiBowater inc.* (2009), 74 C.C.P.B. 239, 57 C.B.R. (5th) 271 (Que. S.C.).

FN68. *Re White Birch Paper Holding Co.*, 2010 QCCS 2590, 82 C.C.P.B. 192, 65 C.B.R. (5th) 186 (Que. S.C.) [*White Birch* (June 2010)].

FN69. *Ibid.*

FN70. *BIA*, *supra*, note 14, s. 60(1.3).

FN71. *CCAA*, *supra*, note 16, s. 6(5).

FN72. *BIA*, *supra*, note 14, ss. 60(1.5) and 60(1.6); and *CCAA*, *supra*, note 16, ss. 6(6) and 6(7).

FN73. Bill C-476, *supra* note 50; (2010), Bill C-487 (2010), *An Act to amend the Bankruptcy and Insolvency Act and another Act in consequence (health-related benefit plans)*, 3rd Sess., 40th Parl., 2010; Bill C-501, *An Act to amend the Bankruptcy and Insolvency Act and other Acts (pension protection)*, 3rd Sess., 40th Parl., 2010; Bill S-214, *supra* note 50; and Bill S-216, *An Act to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act in order to protect beneficiaries of long term disability plans*, 3rd Sess., 40th Parl., 2010.

FN74. Bills C-476 and S-214, *supra*, note 50; Bill C-501 *supra*, note 72.

FN75. Bills C-476 and S-214, *supra*, note 50; Bill C-501 *supra*, note 72.

FN76. Bills C-476 and S-214, *supra*, note 50; Bill C-501 *supra*, note 72.

FN77. *Canada Business Corporations Act*, R.S.C. 1985, c. C-44.

FN78. Bills C-476 and S-214, *supra*, note 51.

FN79. Bills C-487 and S-216, *supra*, note 72.

FN80. At the date of drafting this paper, CAIRP and the IIC had publicized the fact that submission papers had been presented, however the position papers themselves had not been posted on their respective websites. I assume the reader can get access to the position papers by contacting CAIRP at <info@cairp.ca> and by contacting the IIC at <iicinfo@associationsfirst.com>.

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