DAVIES

Davies Restructuring Review 2021: Issue 2

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Emerging Trends for the Short and Long Terms

Canada's economy continues to fare surprisingly well since we published the first issue of our 2021 Restructuring Review in March, despite continuing pandemic restrictions. The Bank of Canada and the Federal Reserve have indicated that lenient monetary conditions and ultra-low interest rates will remain until recovery is well underway. Our U.S. neighbours are well ahead of us in terms of vaccinations and reopening, sparking growing demand since it is a destination for 75% of our exports.

Despite these positives, we have our eye on a number of insolvency and insolvency-related issues. Long-term unemployment is a significant concern given that the number of Canadians out of work for more than six months has been consistently between 1.4 and 1.6 million over the last year – about two-thirds more than when the pandemic started. The struggles of the locked down industries also persist – with employment down 17% in industries as diverse as restaurants and tourism. At the same time, from a business perspective, pent-up demand for travel and hospitality is likely to surge when the economy reopens, matched with Canadian savings at an all-time high. However, any predictions about domestic insolvency rates are challenging, given the inconsistency of vaccine rollouts and the uncertainty about the future course of the pandemic.

Unlike during the global financial crisis, a large uptick in corporate insolvencies has not been a part of the current economic dynamics accompanying COVID-19 globally. At the same time, the low number of insolvency filings is not a sign of corporate health in Canada or elsewhere. As Canada is also somewhat behind parts of Europe in reopening, we have the advantage of more advanced European forecasts. The European Systemic Risk Board (ESRB) set out in its April 2021 risk note four lines of defence against economic and financial instability as the world begins to reopen and government support measures are reduced. The fourth line of defence focuses on efficient and fair insolvency procedures as a key defence against economic costs arising from insolvencies. The ESRB highlights the importance of firms without prospects of

becoming viable again being swiftly wound down and the resources reallocated to more productive uses. In contrast to the observations the ESRB makes about some European countries, we believe Canada is well equipped to counter potential judicial bottlenecks in court filings through the use of effective informal out-of-court and hybrid workout frameworks and the availability of high-quality insolvency practitioners.

In this issue of the *Davies Restructuring Review*, we highlight emerging trends in Q1 data. We saw a considerable increase in the number of filings under the *Companies' Creditors Arrangement Act* (CCAA) in the first quarter, thereby reversing the declining trend that had persisted through the second half of 2020. This reversal was likely a consequence of the prolonged pandemic restrictions, which forced businesses that had previously managed on provisional arrangements to re-evaluate their financial viability and seek formal court protection to work out longer-term solutions. In contrast, the overall numbers of business bankruptcies, proposals and receiverships remained at a level below or comparable to those in 2019 and 2020. We expect that it will take time before the full economic impact of the extended lockdown trickles down through the system.

We also spotlight a key trend that we observed in our analysis of the data on filings in the first quarter: the movement by debtors from the *Bankruptcy and Insolvency Act* (BIA) to the CCAA regime, drawing on the advantages of the flexibility and efficiency afforded by the best aspects of Canada's unique bifurcated insolvency system.

Turning to longer-term trends, we note that the general pace of insolvency law reform and the nature of the current crisis mean that comprehensive reforms to the Canadian insolvency system to respond to the COVID-19 pandemic are unlikely. However, there are a number of tools available to government actors to support corporations and their stakeholders during the insolvency process. In this issue, we take a deep dive into the changing roles and approach of the government as a stakeholder and policy-maker in the Canadian insolvency context.

The Davies Restructuring Review *is a quarterly publication authored by Natasha MacParland, Robin Schwill and Stephanie Ben-Ishai that analyzes key trends and developments in the insolvency and restructuring community.*

Observations of Q1 2021

CCAA PROCEEDINGS

Figure 1: CCAA Restructurings in Canada

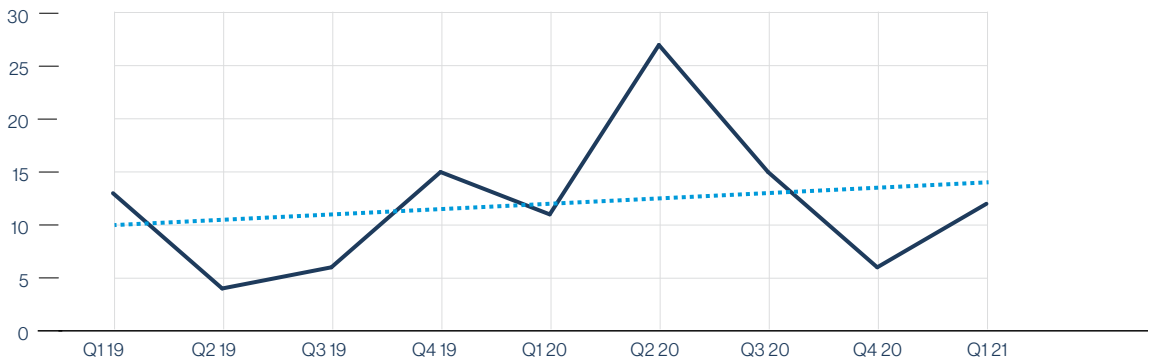
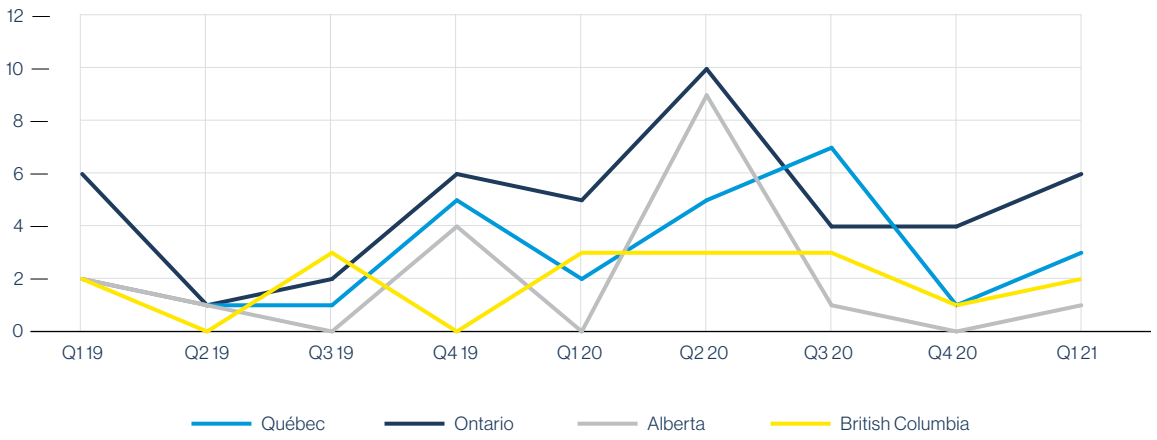


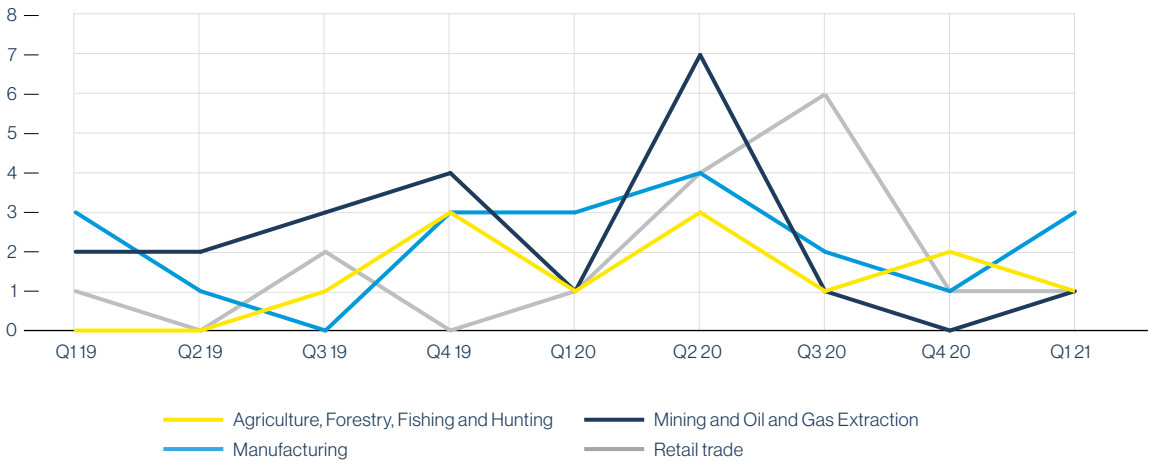
Figure 2: CCAA Proceedings by Province



The overall number of CCAA filings doubled from 6 in the Q4 2020 to 12 in the most recent quarter. The four large provinces all contributed to the aggregate increase; Ontario led the pack with a total of six filings, while Alberta dropped to the bottom of the pack with only one filing in the first quarter of 2021. Within the broader trend, this recent uptick may signal the beginning of a reversal of the steady decline in the number of filings that had characterized the second half of 2020 following a historic high in the second quarter. As we noted in the previous issue of this publication, a likely explanation for the steady decline in the number of filings was the widely held view of many debtors and creditors that the depressed economic conditions caused by the COVID-19 pandemic were temporary. Such belief, in turn, tended to minimize the need to undertake a significant restructuring of businesses.

As the prolonged lockdown continued well into the new year, many businesses were forced to re-evaluate their financial viability. Those that had previously relied on interim financing or entered into temporary private arrangements with their creditors might now have to seek formal court protection to work out a longer-term solution. This likely contributed to the recent rise in the number of CCAA filings. According to Statistics Canada's recent *Canadian Survey on Business Conditions* (with infographics), 39.9% of businesses reported that they were unable to take on more debt in the first quarter of 2021, and only 10.3% reported that they could continue at their current level of revenue and expenditure for the next year before considering closing or filing for bankruptcy. The economic hardship may well continue into the foreseeable future, especially if the Canadian restrictions drag on.

Figure 3: CCAA Proceedings by Sector



As shown in Figure 3, the cross-sectors trend suggests that the impact of the pandemic has not been uniform across industries in Canada. In brief, while manufacturing and mining saw increases in CCAA proceedings in Q1 of this year over the previous quarter, retail trade remained stagnant and agriculture was down.

Following the peak in the number of mining proceedings in the second quarter of 2020, mining has since stabilized and the trend continued well into the first quarter of 2021, with only a small increase over the previous quarter. The high M&A activity in the energy sector at the beginning of the year likely contributed to this trend. Similarly, after retail trade experienced a noticeable increase in the number of proceedings in the second and third quarters of 2020, it has since shown a dramatic decline and remained stagnant over the recent quarter. Manufacturing now tops the chart with three filings and appears to be on track to match its 2020 peak, in part driven by some turmoil in the cannabis sector.

BUSINESS BANKRUPTCIES AND PROPOSALS

The overall number of business bankruptcies and proposals was below or at 2020 figures, and still well below 2019 numbers (see Figures 4-7). The depressed number of filings since the onset of the COVID-19 pandemic may, at first blush, appear counter-intuitive, but it reflects in part the effectiveness of the government's support programs in response to the pandemic. Furthermore, while the prolonged lockdown could be expected to drive up the number of insolvencies, the economic impact may take time to reverberate. The number of court filings and official statistics may also underestimate the actual number of business insolvencies on the ground as many businesses that have failed due to the pandemic restrictions might delay their insolvency filings even if they have permanently shut their doors (e.g., Toronto's Prairie Girl bakery, which shut its doors permanently in January 2021 but had not filed for insolvency by March). Time will tell if the downward trend in bankruptcies as well as the stagnancy in business proposals will ultimately be reversed.

Figure 4: Business Bankruptcies

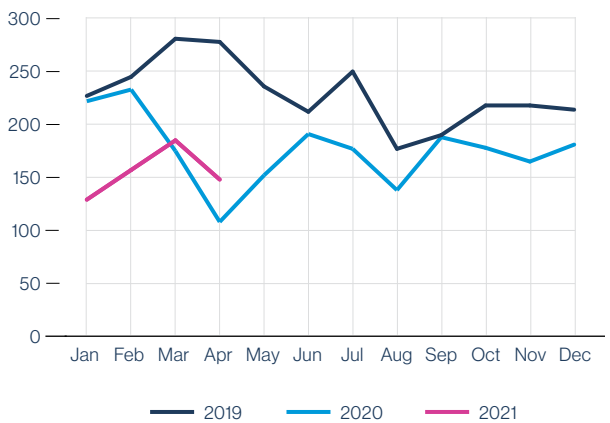


Figure 5: Business Proposals

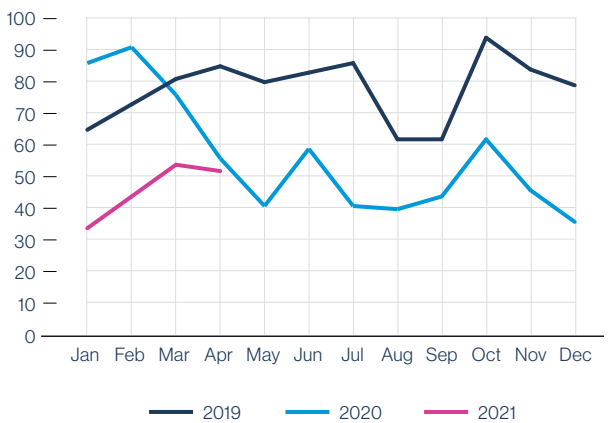
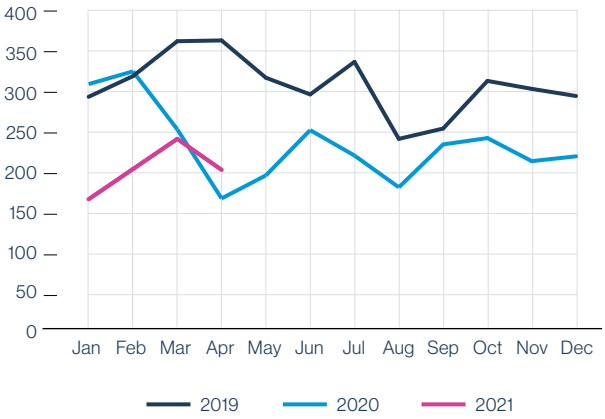
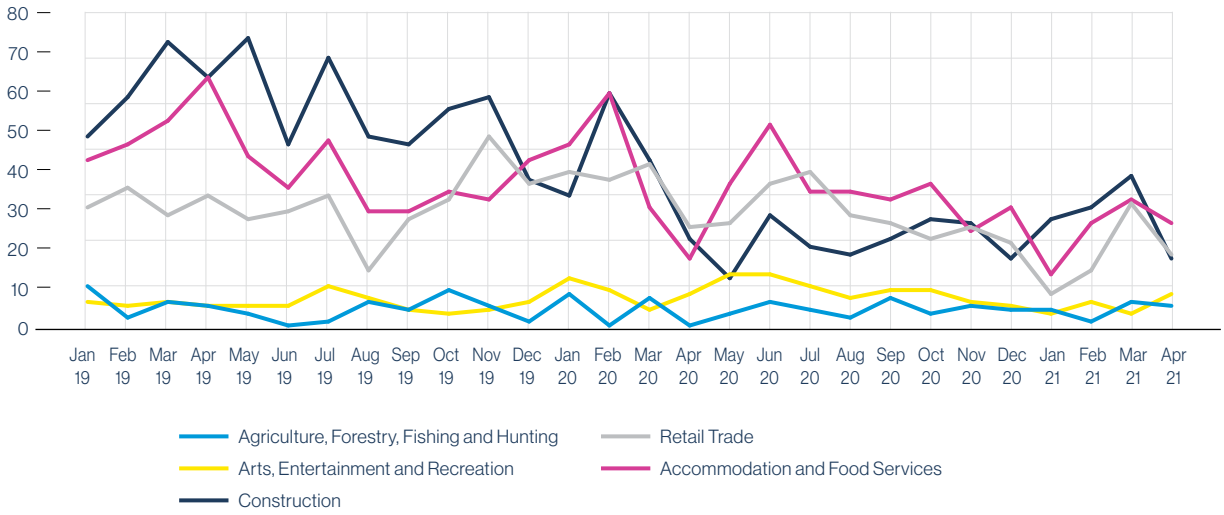


Figure 6: Total Business Bankruptcies and Proposals



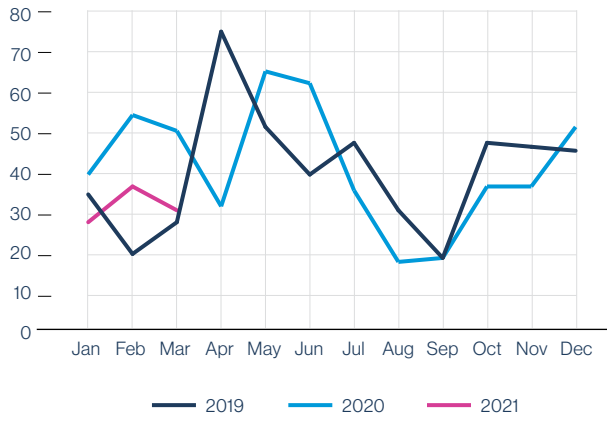
At the industry level, the recent performance of the most affected sectors largely followed their historical trajectories over the last two years. Construction, retail and accommodation continued a downward trend following their 2019 highs. Agriculture and arts also showed some fluctuations within the highs and lows of the previous two years. These cross-sectoral data remain consistent with our overall observation that the pandemic has not caused a spike in the number of business filings in Canada. This holds true at the aggregate and sectoral levels.

Figure 7: Total Bankruptcies and Proposals in Most Affected Sectors 2019-2021



RECEIVERSHIPS

Figure 8: Receiverships in Canada by Volume



The number of receiverships in the first quarter of 2021 remained within the highs and lows of the same quarter in the two years prior to the onset of the COVID-19 pandemic. This trend seems to suggest that business disruptions caused by the pandemic have not had any significant impact on the number of receiverships. Indeed, at a month-to-month level, the slight rise in the number of receiverships in February this year followed by a subsequent decline in March mimicked the trend previously seen in 2020, albeit this year at roughly half the volume.

Figure 9: Court-Appointed Receiverships in Canada by Volume

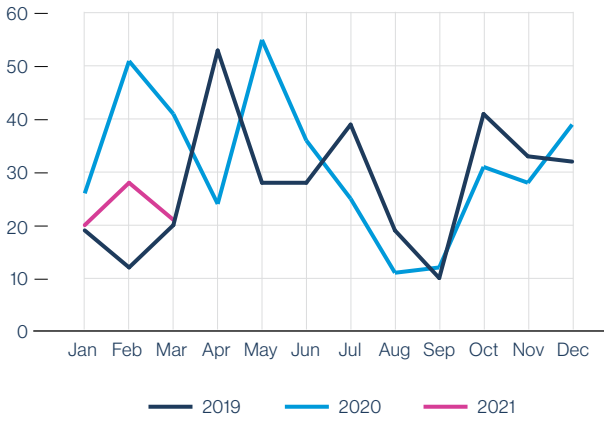
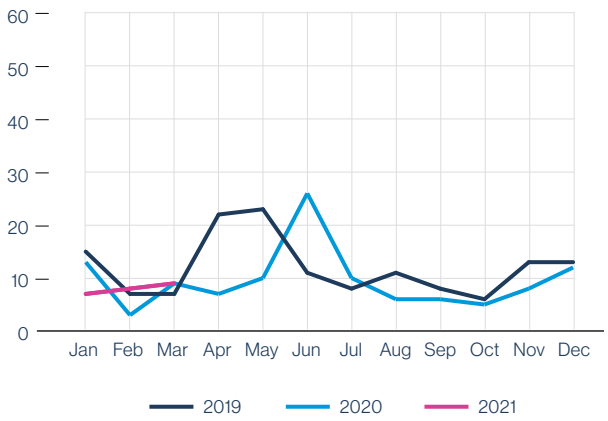


Figure 10: Privately Appointed Receiverships in Canada by Volume



The general observation that business disruptions caused by the pandemic have not had any significant impact on the number of receiverships holds true when we break down the aggregate data further. As shown in Figure 9 above, the volume of court-appointed receiverships in the first quarter of 2021 was within the levels set in the previous two years – slightly higher than the 2019 volume but much lower than the 2020 volume. Similarly, as shown in Figure 10, the number of privately appointed receiverships also remained largely at the same level as in previous years, with the exception of January 2021, when the figure was around half the figures in 2019 and 2020 before rising slightly in subsequent months to match the levels seen in previous years. There were exactly nine privately appointed receiverships in March of both 2020 and 2021.

A Trend to Watch: From BIA to CCAA

In the first quarter of 2021, we witnessed an emerging trend of corporate debtors under the BIA seeking an order authorizing the bankruptcy proceedings to continue under the CCAA. Two debtor companies opted to move from the BIA to the CCAA regime for reasons of flexibility and efficiency. This ship-jumping invites a natural question as to why these two companies did not proceed under the CCAA in the first place. In both instances, they proved to be eligible to proceed under the CCAA. One speculative answer might have to do with the initial desire to avoid the new 10-day stay under the CCAA, which now mandates a more frequent set of court appearances. To these instances we now briefly turn.

CASE EXAMPLE: KANWAL

The first proceeding involved Kanwal Inc. and 9058-0150 Quebec Inc. (Kanwal), which turned to the CCAA to take advantage of the regime's temporal flexibility for filing a plan of arrangement. Kanwal is part of an international group based in Québec that produces specialty rubber and automotive sealing systems.[1] The company first filed a Notice of Intention to Make a Proposal under the BIA in July 2020. However, despite multiple extensions of time for filing a proposal, the company was unable to make a proposal to its creditors before the deadline expired on January 30, 2021. One day before the deadline, on January 29, 2021, the company filed for protection under the CCAA and an initial order was granted. In requesting the continuance under the CCAA, Kanwal sought to obtain additional time that would permit it to finalize its proposed senior secured asset-based financing with Waygar Capital Inc.[2]

1 *Kanwal Inc. and 9058-0150 Quebec Inc.*, Application for an initial order under the CCAA and for the continuation of proceedings commenced under BIA, at para 1.

2 *Ibid* at para 23.

CASE EXAMPLE: ENCOREFX

The second proceeding involved EncoreFX, which turned to the CCAA process after spending a year under the BIA. EncoreFX was in the business of providing foreign exchange risk management and cross-border payment services.[3] Market volatility during the COVID-19 pandemic caused a liquidity crisis that led the company to make a voluntary assignment in bankruptcy under the BIA on March 30, 2020.[4] Over the subsequent year, the administration of the bankruptcy became exceedingly complicated and the Licensed Insolvency Trustee brought numerous applications to address a myriad of issues related to the bankruptcy. Exactly one year after the commencement of the bankruptcy proceedings, on March 30, 2021, the Trustee brought an application to initiate a restructuring under the CCAA.[5] The Supreme Court of British Columbia granted an Initial Order. The Court noted that EncoreFX's overall intention to proceed under the CCAA was to "present a plan of arrangement to the creditors that [would] streamline the proceedings and bring about a more timely resolution of the matter than otherwise anticipated" under the BIA proceedings.[6]

Ultimately, these two proceedings show that the new compressed initial stay might not have dampened the allure of the CCAA process and demonstrate the continued creativity of insolvency practitioners under Canada's unique bifurcated regime.

3 *EncoreFX Inc.*, *Re*, 2021 BCSC 750 at para 1. The CCAA records are available in "EncoreFX Inc.," *Office of the Superintendent of Bankruptcy Canada* (date modified April 6, 2021).

4 *EncoreFX Inc., ibid* at paras 9–11.

5 *Ibid* at para 3.

6 *Ibid* at para 4.

7 Jared A. Ellias and George G. Triantis, "Government Activism in Bankruptcy" (2021) 36 *Emory Bankruptcy Developments Journal* at 4.

A Spotlight on Government Involvement in CCAA Proceedings

We turn next to new U.S. research that has demonstrated that by using the bankruptcy system in a manner similar to investor activism, U.S. governments have, in some instances, gained access to exceptional powers that a debtor enjoys under bankruptcy law in order to facilitate and accelerate policy outcomes. Bankruptcy powers to stay creditor enforcement, break contracts, shed assets and modify obligations can be powerful regulatory tools that governments can harness to accomplish policy objectives. The efficiency gains from proceeding through bankruptcy over the more traditional routes of regulation and appropriation are evident: bankruptcy cases are typically resolved in a far shorter time frame than otherwise required to make legislative changes. Governments may therefore accomplish in a matter of weeks what would otherwise (outside bankruptcy) take years through law-making. Notably, governments could also bypass veto players in the political system and thereby avoid policy paralysis. Finally, the bankruptcy process also benefits from the institutional expertise of lawyers and financial advisers with deep experience in resolving disputes and reaching compromises among reluctant stakeholders.[7]

We highlight below a number of examples of large restructurings in Canada in which various levels of Canadian government were heavily involved in the process and invested in the outcome. Though by no means an exhaustive list, this analysis may provide insight to large entities, government actors and their associated stakeholders in determining the role that the most extraordinary creditor in the economy plays in the next restructuring under the CCAA and the most effective strategies for achieving an optimal outcome for the various actors involved.

GOALS AND METHODS OF GOVERNMENT BANKRUPTCY ACTIVISM

The Traditional Approach: Opting Out

In Canada, as is the case in the United States, the traditional government posture was to try to defend its regulatory authority by "opting out" of bankruptcy law. For example, this was the case in *AbitibiBowater Inc*., in which the province of Newfoundland and Labrador issued environmental protection orders against the company and unsuccessfully argued that the orders were not monetary claims that could be compromised in a corporate restructuring under the CCAA. Similarly, in *Canadian Asbestos Services*, the federal government unsuccessfully argued that it should not be bound by the CCAA and should be paid ahead of the interim lenders for amounts owing for unremitted source deductions under the *Income Tax Act*.

Interestingly, *AbitibiBowater Inc*. set the stage for the government to "opt in" in *Orphan Well Association v Grant Thornton Ltd*. In the latter case, the Supreme Court of Canada held that the Alberta Energy Regulator could impose conditions on the transfer of a bankrupt's licences that required payment or performance of abandonment and reclamation obligations of a debtor. The Supreme Court held that in doing so the regulator was not asserting a claim in the bankruptcy proceeding and was therefore not offending the statutory scheme of distribution established in the BIA. The Supreme Court focused in particular on the fact that the Alberta Energy Regulator was exercising a duty "in the public interest and for the public good" without the expectation of any financial benefit. The result of this was the holding that the abandonment orders were not provable claims and did not interfere with the operation of the BIA.[8]

Most recently, in *Yukon Zinc*, the Yukon Court of Appeal rejected an attempt by the government to opt in with a claim provable in bankruptcy as a result of the failure of the debtor to provide unfurnished reclamation security because that was not a requirement the government could have enforced by legal action. The *Mining Act* does not provide that the government can recover as a debt any required reclamation security that has not been furnished; nor does it provide that the government can otherwise invoke legal process to enforce the obligation to provide required reclamation security. The Court of Appeal distinguished the *Abitibi* test for contingent environmental claims and the requirements for a priority charge in favour of the Crown under section 14.06(7) of the BIA, holding that the latter gives rise to a claim for actual remediation costs and does not refer to costs that may be incurred later.[9]

Government as Interim Lender

At the other end of the pendulum, government actors are increasingly recognizing ways in which they can promote important policy goals by playing a larger role in shaping the outcome of a bankruptcy case. One of the most significant of the bankruptcy features to advance policy goals is interim financing. The financial distress of a debtor's business means that all levels of government can and do provide relief through loans and procurement contracts, and they can condition their financial contribution by tying it to certain policy objectives. Through leverage as an interim lender, government can influence the debtor to (i) assume or reject executory contracts or leases; (ii) sell some or all of its assets; and (iii) restructure its liabilities. Activist investors could use these powers to maximize their private returns, while governments could use these powers to pursue certain policy goals.

8 *Orphan Well Association v Grant Thornton Ltd*. at para 122.

9 *Yukon (Government of) v Yukon Zinc*, 2021 YKCA 2, at para 84. See discussion generally at paras 70–84.

In *Canadian Asbestos Services*, for instance, the government could have used the opportunity to step in as an interim lender. The U.S. bankruptcy case of Johns-Manville, once among the world's largest asbestos miners and product manufacturers, illustrates how bankruptcy can be a forum for broader policy-making. In the midst of a complex restructuring, at the insistence of government stakeholders, the claimants of property damage (those who installed harmful asbestos products that needed to be removed) subordinated their claims to the asbestos health victims on the compelling grounds of morality and policy.[10]

During the global financial crisis, the Canadian government directly stepped in as an interim lender alongside the U.S. government in the Chapter 11 proceedings of Chrysler and General Motors. In the Chrysler case, the U.S. government provided $3.5 billion and the governments of Canada and Ontario contributed a total of $1.45 billion in interim financing. The Section 363 sale of Chrysler under Chapter 11 was unusual in a number of respects, including the fact that the large financial institutions that had a priority claim on Chrysler's assets received 29 cents for each dollar on their $6.9 billion claim, whereas most unsecured, but government-favoured, supplier creditors were paid in full.[11] This illustrates how the governments could become empowered by virtue of their role as interim lenders to determine not only how they would be repaid but also how other stakeholders would be repaid. By influencing the distributional outcome, the U.S. and Canadian governments could promote their policy objectives and prioritize certain stakeholders. In the General Motors case, the financial stakes were even higher – the U.S. federal government provided $30 billion and the Canadian government provided $9.5 billion in the joint interim financing.[12] The U.S. federal government through its task force essentially designed and pushed through the restructuring plan that, in the end, ensured that the workers, suppliers and secured bondholders – which held a very small fraction of the company's outstanding debt – were adequately compensated, while the unsecured bondholders – which held the majority of the outstanding debt – were left with worthless claims against the residual assets not transferred into the new entity.

By influencing the distributional outcome, the U.S. and Canadian governments could promote their policy objectives and prioritize certain stakeholders.

10 *Supra* note 7; see also, Donald R. Korobkin, "Rehabilitating Values: A Jurisprudence of Bankruptcy" at 755–59.

11 Mark J Roe and Joee-Hee Chung, "How the Chrysler Reorganization Differed from Prior Practice" (2013) *Journal of Legal Analysis* 399 at 400; Stephen B. Selbst, "General Motors and Chrysler: The Changing Face of Chapter 11" *Commercial Lending Review* (November-December 2009) at 4.

12 Selbst, *ibid* at 7.

Restructuring Industries and Institutions

In *Canadian Red Cross Society* as well as the more recent CCAA proceedings involving asset backed commercial paper (ABCP), the federal government, working with provincial governments, used the CCAA process to restructure and save entire industries.[13] Both cases demonstrate that governments may involve themselves in restructuring proceedings, as creditors or stakeholders, not only to minimize their own potential liability but also to ensure that public policy objectives are achieved – whether to ensure that a new blood system is properly in place to serve the public or to prevent the collapse of an entire industry from injecting further instability into the market in the midst of a global credit crunch. In *Canadian Red Cross Society*, the Red Cross collapsed in Canada after it was the target of approximately $8 billion in claims from those who contracted diseases from receiving infected blood products during the 1980s – a case that became known as the "tainted blood scandal."[14] The result of the restructuring plan was to require the Red Cross to sell and transfer its de facto monopoly to administer the Canadian blood system to Héma Québec and Canadian Blood Services – two newly formed government agencies that together formed a new national blood authority.[15] Heavy government involvement in the process was required to ensure that all the necessary approvals were obtained to implement the plan and that an essential program continued operating.

In the *ABCP case*, financial support from Canadian governments was essential to the viability of the plan to restructure the ABCP market. The collapse of the ABCP market in late 2007 instantly wiped out more than $32 billion in ABCP held mostly by institutional investors and dealers in Canada. This paved the ground for what was to become Canada's largest corporate restructuring of an entire market in a single CCAA proceeding. The CCAA process was initiated by a band of major holders of ABCP who proposed a conversion of the outstanding, illiquid ABCP notes into long-term bonds. Although the final terms of the plan were upheld by the courts and survived various appeals,[16] one major obstacle to implementation was that the rising turmoil in the financial market had caused the credit spreads to move apart to record levels requiring an additional $4.5 billion to be in place to support the leveraged credit default swaps contemplated under the restructuring. The governments of Canada, Québec, Ontario and Alberta came to the rescue and facilitated the successful

In *Canadian Red Cross Society* as well as the more recent CCAA proceedings involving asset backed commercial paper, the federal government, working with provincial governments, used the CCAA process to restructure and save entire industries.

13 *Canadian Red Cross Society*, 1998 CanLII 14907 (Ont SC). *Metcalfe & Mansfield Alternative Investments II Corp (Re)*, 2008 CanLII 27820 (ONSC), aff'd 2008 ONCA 587, leave to appeal refused 2008 CanLII 46997 (SCC) [*ABCP case*].

14 *Canadian Red Cross Society, ibid* at para 2.

15 *Ibid* at para 6.

16 *Metcalfe & Mansfield Alternative Investments II Corp (Re)*, *supra* note 13.

conclusion of the restructuring process in 2009. In so doing, the governments did not only contain the repercussions of the ABCP market collapse but also ensured that retail investors, which formed a small part of the ABCP noteholders, would receive immediate payout. Most of these retail investors had struck separate deals with their dealers, but the payment hinged upon the completion of the main restructuring.

Moving away from the financial services context, the Christian Brothers of Ireland in Canada (Christian Brothers) was incorporated under an Act of Parliament in 1962 and was granted permission to operate "schools, educational institutions and orphanages in various parts of the country."[17] Christian Brothers was wound up after many claims were made stemming from decades of abuse of men and boys at the Mount Cashel Orphanage in Newfoundland. In this scenario, the involvement of the government of Newfoundland and Labrador served a two-fold purpose of ensuring adequate compensation for victims while limiting its own liability.[18] The government achieved its objective by supporting maximum compensation for victims through the restructuring process, thus aligning its legal position with public policy objectives.

Turning next to the constantly evolving science of human health, which poses risks to businesses selling consumable products: what is harmless today might be harmful tomorrow. The consumption of tobacco products and the related class action lawsuits are likely to serve as a point of interest in the history of the corporation. In Canada, the three largest tobacco companies filed for creditor protection following the affirmation on appeal in 2019 of a 2015 Québec Superior Court judgment holding that they were jointly and severally liable for a maximum payout of $13.6 billion to Québec plaintiffs for damages caused by the consumption of tobacco products. Meanwhile, various levels of government, including all 10 provincial governments, are currently involved as tax creditors in ongoing proceedings against the tobacco companies and, more significantly, also as plaintiffs with "Medicaid" actions seeking to recover healthcare costs incurred in treating smoking-related diseases, totalling in excess of $500 billion.[19]

Transforming Governance Structures

Various levels of Canadian government have also played an active role in transforming the governance structures of insolvent companies through the CCAA process. In *Stelco*, as part of a first attempt to successfully emerge from CCAA protection through a plan of arrangement, Stelco negotiated an agreement with the province of Ontario that required, among other items, that the court order sanctioning the final plan name the members of Stelco's board of directors and such members must be approved by the province. The Court of Appeal upheld this key provision.[20] The Ontario government's key policy objective was to ensure that the new governance structure of the restructured entity would take into account the interests of Stelco employees and unionized pensioners whose interests the province was trying to protect. In a more recent Stelco restructuring, in 2017 Stelco emerged with a restructuring plan that involved significant arrangements with the province of Ontario to address environmental obligations enabling the acquisition of Stelco by its new owner, Bedrock Industries, LP.

17 *Christian Brothers of Ireland in Canada (Re)*, 2000 CanLII 5712 at para 2.

18 *Ibid* at para 15.

19 Imperial Tobacco – Monitor's Pre-filing Report (12 March 2019) at paras 7, 39.

20 *Stelco Inc., Re*, 78 OR (3d) 254, 2005 CanLII 40140 (ON CA) at para 6.

The federal government played a similar role in the wake of the Lac-Mégantic rail disaster. On July 6, 2013, the downtown core of a small municipality in Québec was devastated when 72 railway tankers filled with crude oil derailed and exploded, setting buildings on fire and killing 47 people in what was the fourth-deadliest railway disaster in Canadian history. In addition to the fire and deaths, approximately 100,000 litres of crude oil spilled into the Chaudière River. Montreal Maine & Atlantic Railway Co. (MMA), facing lawsuits from victims and governments, and without adequate insurance to cover the estimated liabilities, was forced into insolvency. In the aftermath of the railway disaster, there was widespread dissatisfaction with the partial making-whole of the victims and the environment. This prompted the Canadian government to take subsequent legislative action to reform the industry by creating a pooled insurance fund, premised upon achieving three policy objectives – namely, to compensate victims; pay for cleanup costs; and protect taxpayers. In 2015, the *Safe and Accountable Rail Act* was passed. The Act requires railway companies to increase the minimum amount of liability insurance they carry and pay a mandatory amount of fee into a pooled fund to cover the costs of damages that exceed their insurance policy.

CASE EXAMPLE: AIR CANADA INC.

In *Air Canada*, a proceeding invoking policy issues associated with the importance of a national air carrier, the Ontario Superior Court of Justice held that a monetary penalty under the *Aeronautics Act* issued against Air Canada by the Minister of Transport prior to its CCAA proceedings was a claim in the CCAA proceedings and was therefore a compromised debt after the plan received court sanction.[21] The Court rejected the Attorney General's argument that the penalty was not a claim because the Crown was not acting in a commercial capacity or "attempting to make money" when it enforced sanctions against an offender like Air Canada.[22]

The Court further determined that the monetary penalty was a claim provable in bankruptcy and should be dealt with through the CCAA process. Moreover, the Court observed that the CCAA was not a "free pass" or "pardon" for regulatory offences committed prior to initiating the CCAA proceeding because the government was entitled to file its claim with the claims officer, vote on the subsequent plan and receive a distribution under the plan (even if it may not always collect the full amount). Indeed, the Court pointed to several regulators filing claims during the CCAA process and reaching a resolution prior to Air Canada's emergence from court protection.[23] A further issue considered by the Court was whether the monetary penalty was an "excepted claim" under the BIA. The Court answered in the negative. The Court was of the view that section 178 of the BIA did not apply. The Court held that the CCAA refers to the BIA solely for the purpose of determining what is or is not a "claim" but the CCAA does not require a court to determine whether a claim is an excepted claim under section 178 of the BIA; nor does the CCAA itself contain a provision analogous to this aspect of section 178 of the BIA.[24]

21 *Air Canada (Re)*, 2006 CanLII 42583 (ON SC), at paras 32–33.

22 *Ibid* at paras 19–23.

23 *Ibid* at paras 24–30.

24 *Ibid* at paras 34–35.

Concluding Thoughts

In summary, American commentators have observed that over the past quarter century, private investors – through strategies that have been termed "bankruptcy activism" – have become increasingly sophisticated in harnessing bankruptcy rules that affect the finance, governance and operations of firms that file under Chapter 11. Governments too, they observed, have gradually moved from a defensive to an activist posture in the bankruptcy context in order to exploit analogous opportunities to pursue their policies and political objectives.[25]

In our experience representing actors in most of the proceedings described to this point, we have observed a similar shift in the Canadian context in which Canadian governments have taken on an active role as a player alongside U.S. governments in cross-border reorganizations and in their own right. Our review has shown how Canadian governments have leveraged their financial and political weight to inject themselves into the restructuring processes of numerous large corporations and organizations since the 1990s. Against this historical backdrop, the extensive governmental intervention and financial spending of governments across the world during the global financial crisis and, currently, the COVID-19 pandemic, are not isolated phenomena witnessed only in times of national emergency. The Canadian insolvency system has a key role to play as governments and other stakeholders take actions to prevent economic and financial instability as our country begins to reopen.

Our review has shown how Canadian governments have leveraged their financial and political weight to inject themselves into the restructuring processes of numerous large corporations and organizations since the 1990s.

25 *Ibid* at para 52.

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