



INSOL INTERNATIONAL
FOUNDATION
CERTIFICATE
IN INTERNATIONAL INSOLVENCY LAW

$$10 + 8.5 + 14 + 15 = \frac{47.5}{50}$$

SUMMATIVE (FORMAL) ASSESSMENT: MODULE 4C

CANADA

This is the **summative (formal) assessment** for **Module 4C** of this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

The mark awarded for this assessment will determine your final mark for Module 4C. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT

Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.
2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way. DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.
3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).
4. You must save this document using the following format: **[studentID.assessment4C]**. An example would be something along the following lines: 202122-336.assessment4C. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentnumber” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words.**
6. The final submission date for this assessment is **31 July 2022**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
7. Prior to being populated with your answers, this assessment consists of **7 pages**.

ANSWER ALL THE QUESTIONS

10

QUESTION 1 (multiple-choice questions) [10 marks in total]

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and mark your selection on the answer sheet by highlighting the relevant paragraph in yellow. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

Question 1.1

Which branch of the Canadian government has the exclusive power to make laws in relation to bankruptcy and insolvency? Indicate the correct answer from the options below.

- (a) Federal. ✓
- (b) Provincial.
- (c) Municipal.
- (d) The power is shared between the three levels of government.

Question 1.2

Which federal statute governs the bankruptcy regime in relation to an individual bankruptcy? Select the correct answer from the options below.

- (a) the Bankruptcy and Insolvency Act (BIA). ✓
- (b) The Companies' Creditors Arrangement Act (CCAA).
- (c) The Winding-up and Restructuring Act.
- (d) The Canada Business Corporations Act (CBCA).

Question 1.3

Which of the following is incorrect with respect to proceedings under the CCAA?

- (a) The CCAA is a debtor-in-possession restructuring statute.
- (b) The CCAA is available to companies with debts less than CAD 5 million. ✓
- (c) The CCAA is a federal statute. ✓
- (d) The CCAA sets out a relatively skeletal framework, and affords broad discretion to a judge as compared to a restructuring under the BIA.

Question 1.4

Select the **best answer** from the options below.

The purpose(s) and objective(s) of the BIA is to:

- (a) provide for the financial rehabilitation of insolvent persons.
- (b) allow for an investigation to be made into the affairs of a bankrupt.
- (c) provide a collective proceeding for orderly and fair distribution of property of a bankrupt among unsecured creditors on a *pari passu* basis.
- (d) All of the above. ✓

Question 1.5

Which of the following is **not** an “act of bankruptcy” listed in section 42 of the BIA?

- (a) the debtor makes an admission of his / her inability to pay debts.
- (b) the debtor ceases to meet liabilities generally as they become due.
- (c) the debtor makes an assignment of property to a trustee for the benefit of creditors.
- (d) the debtor misses a mortgage payment. ✓

Question 1.6

Indicate the **correct answer**:

Under Canadian law, when a company enters the “zone of insolvency”, the directors of a company:

- (a) continue to have a fiduciary duty to act honestly and in good faith with a view to the best interests of the company. ✓
- (b) no longer have a fiduciary duty to act honestly and in good faith with a view to the best interests of the company.
- (c) cannot be held personally liable for any of the company’s debts.
- (d) cannot consider, under any circumstances, the interests of creditors, consumers, governments, employees, or any other stakeholder in discharging their duties.

Question 1.7

Indicate whether the statement below is **True or False**:

It is possible to fund continued operations during restructuring proceedings in Canada.

(a) True. ✓

(b) False.

Question 1.8

Indicate whether the statement below is True or False:

Upon bankruptcy, the debtor ceases to have the legal right to deal with its property.

(a) True. ✓

(b) False.

Question 1.9

Indicate whether the statement below is True or False:

There is no automatic stay of proceedings upon entering bankruptcy proceedings.

(a) True.

(b) False. ✓

Question 1.10

Indicate whether the statement below is True or False:

Foreign creditors and Canadian creditors participate equally in a bankruptcy and no distinction is made between them.

(a) True. ✓

(b) False.

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 3 marks]

8.5

Identify the conditions set out by the Supreme Court of Canada for a claim to be provable in bankruptcy under the BIA.

- 121(1) of the BIA provides for claims to be provable. It provides that "All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act".

3

- The Supreme Court in the case of *Newfoundland and Labrador v AbitibiBowater Inc* [2012] held that for a claim to be provable in bankruptcy under the BIA, it must meet the following conditions – (a) the debt and liability must be owed to the creditor (b) the debt and liabilities must be incurred (existed) before the debtor becomes bankrupt and (c) the debt and liabilities must be ascertainable in monetary value.

Question 2.2 [maximum 2 marks]

Generally, in the context of an individual bankruptcy, what type of assets can a debtor keep in a bankruptcy?

2 Generally, the type of assets that a debtor can keep relates to assets that are reasonably needed for “living / livelihood”. They include (a) personal items and clothing (b) household items such as furniture and food (c) tools necessary for debtor’s work (earning a living / livelihood) (d) motor vehicle up to a certain value and (e) certain farm property.

Question 2.3 [maximum 3 marks]

Name three methods for entering into bankruptcy.

The three methods are (a) Involuntary bankruptcy (b) Voluntary bankruptcy and (c) Failure to perform the terms of a BIA proposal

Involuntary bankruptcy – It is initiated by creditor(s). The elements in which a creditor must prove include the debtor (a) owing more than CAD 1,000 of unsecured debt (b) providing evidence that the debtor has committed an act of bankruptcy.

2.5 Voluntary bankruptcy – It is “initiated” by the debtor himself. To qualify for this, the debtor must fall within the definition of “insolvent person”. An “insolvent person” (a) is a person who owes creditors more than CAD 1,000 (b) is not able to pay debts as they fall due and (c) the aggregate liabilities exceed assets.

Failure to perform the terms of a BIA proposal – If a debtor defaults or fails to perform according to the terms of the BIA proposal, the proposal trustee must inform the creditors and the Official Receiver. A motion will be brought to the court for a decision – whether to annul the proposal. If the court annuls the proposal, the debtor will be made a bankrupt (automatically).

ALSO -
↳ negative vote!

Question 2.4 [maximum 2 marks]

What is the definition of “debtor” in section 2 of the BIA?

Section 2 defines

- debtor as "includes an insolvent person and any person who, at the time an act of bankruptcy was committed by him, resided or carried on business in Canada and, where the context requires, includes a bankrupt" *define.*
- person as "includes a partnership, an unincorporated association, a corporation, a cooperative society ..."
- corporation as "a company or legal person that is incorporated by or under an Act of Parliament ..."

A debtor therefore can be (includes) an individual, a company, partnership, an unincorporated association and a corporation.

QUESTION 3 (essay-type questions) [15 marks in total]

Question 3.1 [maximum 8 marks]

What is the difference between a private receiver and a court-appointed receiver?

In your essay you should refer to at least the following: (1) how each type of receiver is appointed, (2) the duties of each type of receiver, and (3) the circumstances in which each type of receiver is generally used.

Difference between a private receiver and a court-appointed receiver

- Private receiver - In a business arrangement between a debtor (example - borrower) and a creditor (example - lender), a contractual arrangement (security agreement) may provide for the appointment of receiver (private receiver) in the event of default of the security agreement (often, defaults include failure to pay the debt as it falls due). This is a private contractual rights and obligations agreed between the parties. The appointment and the receivership process generally does not involve the court. It is generally regarded as a cost effective and quick recovery process. However, it can be costly and messy if the receivership appointment (or acts of the private receiver) is contested by the debtor
- Court-appointed receiver - Section 243(1) of BIA provides that "... on application by a secured creditor, a creditor may appoint a receiver to do any or all of the following if it considers it to be just and convenient ... (a) take possession of all or substantially all of the inventory, accounts receivable or other property of an insolvent person or bankrupt ... (b) exercise any control that the court considers advisable over that property and over the insolvent person ... and (c) take any other action that the court considers advisable. Therefore, the appointment is by the court on the application of a secured creditor and the court may appoint a receiver if it thinks "just and convenient". The powers of the receiver will also be provided by the court.

How are they appointed

- Private receiver is appointed by the holder of security agreement (often, a lender). Circumstances (event of default) that allow for the appointment of private receiver will be set out in the security agreement. Event of default (failure to pay debt will be one of the events

of default) must be triggered before the holder of the security agreement (lender) can appoint a private receiver. Procedural requirements set out in the security agreement must be observed. For example, if the lender is required to give notice to before it appoints a private receiver, the lender must give notice. Contractual rights and obligations of the parties must be observed.

- Court-appointed receiver is appointed by the court on the application of a secured lender if the court thinks it is just and convenient: s 244 BIA. A statutory notice (10 days) must be provided to the debtor when the secured creditor wants to enforce its security: s 244 of the BIA.

Duties

- The private receiver, when appointed, has primary duties to the secured creditor who appointed him under the security arrangement. However, he must act honestly and in good faith and has duties to maximize return (obtain the best possible price on assets sale).
- ✓ • A court-appointed receiver is an officer of the court. He has duties to all creditors, not to the creditor who made the application to the court for his appointment. He reports to the court and takes direction from the court.

Circumstances in which each type of receiver is used

- Private receiver - It is generally useful (it is cost effective and a quick recovery process) for smaller businesses, non-complex and non-contested cases. The appointment of a private receiver may be contested by the counterparty (debtor) in court. This makes it messy and calls into question (legality) of his appointment, and consequently the legality of actions (business decisions) taken by him. It is therefore generally used for smaller and (potentially) non-contested cases.
- ✓ • Court-appointed receiver – It is generally used in more complex cases, especially if the secured creditor feels that the private receiver appointment will be contested. Court appointment provides a greater degree of comfort as it takes the issue of legality (allegation of illegality) of private receiver appointment out of the question. The receiver appointed by the court need not worry about his professional liability (as compared to a private receiver appointment). The creditors and suppliers who continue to have business relationship with the court appointed receiver need not worry about the legality of his appointment and the contractual arrangement as may be made by the creditors and suppliers with the court appointed receiver. Further, the court-appointed receiver may apply to the court for assistance in relation to carrying out his duties, thus “insulating” him from liability. For example, he may reach out to the court to seek approval of the court to sell the business at a certain price which he thinks is fair and reasonable. The potential purchaser who buys the business (with the approval of the court) need not worry about the validity of the sale. Other advantages of the court-appointed receiver are (a) on appointment, a stay of proceeding may be granted thus rendering *ipso facto* clause to be “not enforceable” during the stay. This is a huge advantage if the debtor (in the interest of the business) needs the continuing

supplies from the supplier who has the contractual rights to invoke the *ipso facto* clause and (b) where financing is needed, court appointed receiver can borrow money on a “super-priority” basis.

Question 3.2 [maximum 7 marks]

Write a short essay that identifies the main policy goals of the Canadian insolvency regime and provide examples of how these policy goals are reflected in different aspects of the insolvency system. In your essay, explain why the national insolvency system in Canada is described as following a “single proceeding” model.

Policy Goals

- Canada’s insolvency regime strikes a balance between reorganisation (with the view of rehabilitating a distressed debtor) and liquidation (where there is no business case for the company to be rehabilitated or “turnaround”). Reorganisation is preferred as it is likely to preserve the business value (as opposed to liquidation) by keep the business alive, thus generating economic activities, saving jobs, providing employment income. However, it also recognises the creditors rights; allowing secured creditors to enforce their securities and unsecured creditors to enforce their rights. The balance between reorganisation and liquidation are reflected in various insolvency regime (systems) and they are explained below.

Aspects of insolvency system (regime) that reflects the balance between reorganisation and liquidation

- BIA - Corporate and personal bankruptcy.
 - BIA is a comprehensive legislation that provides for an orderly liquidation of an insolvent person (example, company and individual).
 - To the extent that a person (company or individual) is insolvent, BIA provides for a collective proceeding such that assets will be realised by the trustee and the proceeds distributed to creditors, according to their statutory entitlements.
 - To the extent that the insolvent person could be rehabilitated, BIA contains provisions for rehabilitation. During this process, protection (stay) will be granted, and creditors are not able to take proceedings against the debtor, giving the debtor a “breathing” space to reorganise its affairs.
 - However, secured creditors are not subject to the stay unless the court orders otherwise. Effectively, the secured creditors can proceed to realise the security. This provides a balance between the needs of the debtor and creditor.
 - In relation to individual bankruptcy, certain assets are exempted (debtors will keep the assets) from being placed in the bankruptcy estate. These assets are generally those that the individual need to main a “basic standard of living or earning a

6

livelihood” such as personal clothing, household furniture and food, tools necessary for the debtor’s work.

- Other protections afforded to a bankrupt individual include (a) he cannot be deprived of public utilities service merely because he is a bankrupt or for amount owing before he was made a bankrupt (b) ipso facto clauses cannot be applied and (c) an individual bankrupt is automatically discharged (if conditions are met) after a certain period of time (as set out in the IBA); it is an opportunity for him to start afresh, without being burdened by past debts.
 - To protect creditors, certain fraudulent and preference transactions (transaction at an undervalue for example) which are against the collective interests of creditors can (may) be voided by the court.
-
- WURA – This is a special federal legislation covering certain types of corporations, broadly covering insolvency of bank, trust, and insurance company. Insolvency of such companies has systemic (knock-on) effects on other companies and potentially create market (financial) disruptions. Understandably, a special legislation is needed for such companies, providing a balance protecting the market (financial) system and interest of the creditors.
 - Receivership – Receivership can take the form of private receiver appointment or court-appointed receiver. Broadly, the receivership regime is creditors friendly, allowing a secured creditor to enforce its right “privately” or through the court.
 - CCAA – This is a “debtor friendly” regime focusing on corporate rescue. The primary driver is to give a distress debtor breathing space to carry out a reorganisation so that business can be kept alive. While breathing space is given to the debtor to reorganise itself (for example, a stay may be granted by the court), there are also safeguards for creditors. For example, a reorganisation scheme can only be binding only if certain requisite majority is achieved (voted in favour by the creditors / classes of creditors). CCAA may also be used for group of debtor companies, thus providing opportunities for the group to be kept alive, while the creditors rights are “temporarily suspended” under the stay order. Another safeguard provided to the creditors is the appointment of a “Monitor”, who is a licensed insolvency professional and a court officer, who plays a supervisory role of the reorganisation scheme, ensuring that the interests of the creditors are safeguarded.
 - Debt restructuring under CBCA – Another avenue (insolvency regime) available to a distressed / insolvent debtor is to resort to provisions under CBCA to carry out a reorganisation.
 - Cross border insolvency law – Canada is a trading nation, and it recognises the need to address the issue of cross-border insolvency and an orderly conduct of insolvency process. It has adopted the UNCITRAL Model Law (although modified). In brief, the Model Law recognises the rights of creditors and at the same time, it recognises the need for a debtor to be protected while it attempts at re-organisation.

Single Proceeding Model

- In Canada insolvency proceeding, creditors remedies are placed in a single proceeding. For example, when a trustee is appointed in a bankruptcy proceeding, other proceedings against the debtor is stayed except with leave of court. Claims of the creditors are (collectively) adjudicated by the trustee. Creditors are not allowed to pursue separate legal proceedings against the debtor, which will cause value destruction.
- The trustee establishes (adjudicates) the amount owing to creditors via proof of debt (claim) exercise, without the need of the creditors going to court to establish the claim, unless there is a dispute to the claim between the creditor and trustee, and that a court decision is needed. The claims by creditors are collectively established (admitted) by the trustee.
- The trustee will liquidate the assets, collect the proceeds, pay the money collected to the creditors (collectively) according to their statutory entitlements. Unsecured creditors will share the proceeds on pari passu basis.

QUESTION 4 (fact-based application-type question) [15 marks in total]

Question 4.1 [maximum 15 marks]

You are a lawyer in Canada. You are consulted by counsel in a foreign jurisdiction who is representing an agent operating under the law of the foreign jurisdiction and who is empowered by the legislation and courts of that foreign jurisdiction to deal with the assets of insolvent companies. The online seller has a fulfilment office and warehouse in Canada. The foreign agent has taken control of the assets of an online seller of clothing with a head office that is registered in the foreign jurisdiction where senior management of the company have their offices. The business sells clothing around the world, including to customers in Canada. Due to currency exchange- and supply-related issues, the company has been unable to maintain liquidity and has defaulted on various loans to its foreign-based secured lenders who are owed in excess of CAD 200 million and, as a result, has stopped fulfilling orders in process, including to Canadian customers. As a result, a class action lawsuit has been filed by a Canadian law firm seeking damages on behalf of customers for monies paid in respect of unfulfilled orders in the amount of CAD 2 million. That lawsuit in Canada is still in the pleadings phase. It also appears that the Canadian resident in charge of the fulfilment office and warehouse in Canada may have been diverting funds improperly. The foreign agent wants to further investigate. The foreign agent consults you about seeking recognition of the foreign proceeding in Canada in order to maximise recoveries and provide for an equitable distribution of value among all creditors.

Using the facts above, answer the questions that follow.

Question 4.1 [maximum 5 marks]

The foreign agent wants to understand the process to commence a recognition application and obtain recognition of the foreign proceeding in Canada. What is your advice?

- Canadian law (under BIA and CCAA) recognises foreign insolvency proceedings if elements to the recognition are met. The elements are (a) it must meet the statutory definition of foreign proceeding and (b) it must meet the statutory definition of "foreign representative,

and (c) whether the foreign proceeding is a “foreign main proceeding” or “foreign non-main proceeding.

- Broadly, Canadian judges are inclined and have wide discretion in relation to how they view the elements - whether it meets the statutory provisions of “foreign proceeding” and “foreign representative”. Canadian courts to-date have been inclined to accept cross-border insolvency proceeding orders. In the absence of evidence to the contrary (for example, the foreign insolvency order was obtained by fraud, or it is manifestly against the public policy in Canada or where there is lack of natural justice), it is likely that the foreign proceeding will be recognised in Canada.
- On the basis that there is no issue in relation to “foreign proceeding” and “foreign representative (being validly appointed) elements, the next issue to determine is whether the foreign proceeding should be recognised in Canada as a foreign main proceeding or foreign non-main proceeding.
- There is a rebuttable assumption that COMI is the place of the registered office. In *Re Mt Gox* [2014], the court laid down three key points in considering the COMI of the debtor – they are (a) the location of the significant creditors (b) the location of debtor’s key assets and (3) the location of the debtor’s headquarters or its nerve centres.
- On the facts, the registered office is in the foreign country. The total debt in Canada is CAD 2 million against CAD 200 million of foreign secured debts and (c) the office in Canada relates to “fulfilment and warehouse”. The foreign representative (agent), on the facts, suggest that he has taken control of the assets of the online seller in his jurisdiction where the head office and its senior management of the company have their offices (likely to be the nerve centre). It is also assumed (not stated in the facts of the case) that the debt of CAD 200 million is also owed in that foreign country.
- On this basis, COMI is in the foreign country and if it is recognised in Canada, it will be recognised as a foreign main proceeding.
- If it is not recognised as a foreign main proceeding (for whatever reason), it is possible that Canada may recognise the foreign insolvency proceeding as foreign non-main proceeding. For foreign non-main proceeding, Canada employs a different definition (criteria) in determining whether it is a foreign non-main proceeding. It uses “real and substantial connection” criteria as opposed to the concept of “establishment” under the UNCITRAL Model Law on Cross-Border Insolvency.

Question 4.2 [maximum 5 marks]

The foreign agent wants to understand whether or not you believe the foreign agent can obtain a stay of the Canadian litigation and why. What do you tell the foreign agent?

- If the foreign representative can persuade the court in Canada that it meets the elements mentioned above, the foreign proceeding is likely to be recognised in Canada as a foreign main proceeding.

- The legal consequence, if it is recognised as a foreign main proceeding, is that there will be an automatic stay of Canada legal actions – the class action lawsuits filed by the Canadian lawyer for unfulfilled orders in Canada will be stayed.
- However, if the Canadian court decides that it is not a foreign main proceeding, the Canadian court may (can) recognise it as a foreign non-main proceeding.
- If it is a foreign non-main proceeding, the stay is not automatic, but the foreign agent can still apply for the stay. The request for the stay must be requested and the foreign representative must provide reason(s) and justify for them.
- Once the foreign insolvency proceeding is recognised, it gives the foreign representative a standing in the Canadian court – for him to appear and be heard.
- If the foreign representative can satisfy the court that the stay is necessary “for the protection of the debtor company or in the interest of creditors” the court in Canada may make “any order that it considers appropriate”: s 272 CCAA. This includes a stay order.

Question 4.3 [maximum 5 marks]

The foreign agent wants to know whether the Canadian court is limited to Canadian entitlements and remedies in the relief they can provide? What do you tell the foreign agent?

- 5
- As mentioned above, BIA and CCAA provide the Canadian court with wide discretions to issue “any order it considers appropriate”. This includes an order compelling the witnesses in providing information, co-operation, and providing documents as the court considers appropriate: s 272 CCAA.
 - On the facts, it is noted that the fulfilment office and warehouse in Canada may have been diverting funds improperly and that foreign agent wants to further investigate. The foreign agent may request the court to issue an appropriate order to investigate the diversion of funds – this may include compelling the witnesses to co-operate, provide information and documents relating to the debtor’s assets and affairs.
 - The court in Canada has wide discretion – it is not limited to providing remedies that are typically available in Canada. In the case of *Re Hartford Computer Hardware Inc* [2012], the court ordered a relief where it is not ordinarily available in Canada. In that case, the court approved a DIP financing arrangement that contains a “roll-up” provision relating to pre-petition secured debt.

*** End of Assessment ***