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• RECEIVERSHIP ORDERS — WHERE DO WE GO FROM HERE? •

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Since the early 1990s the use of court-appointed receivers has increased dramatically. This may be due to the fact that in the early 1990s the provisions of the *Bankruptcy and Insolvency Act*¹ (the “BIA”) were expanded to provide receivers with increased powers and a “Commercial List” was established in Toronto to hear receivership and certain other commercial matters (the “Commercial List”). The BIA amendments gave insolvency practitioners broad discretionary language on which to rely in order to persuade courts to include expansive powers in receivership orders and the Commercial List provided sophistication for commercial judges who are willing to grant these orders to maximize realizations for creditors.

Recently, the use of broad receivership orders has come under increased judicial scrutiny. Some courts have now pushed back and are asking that parties justify this broad relief. In particular, the Ontario Court of Appeal has indicated that Ontario courts are not authorized to grant certain protections which had previously been regularly granted. As a result, insolvency practitioners will have to take a hard look at the powers that the courts will grant to a receiver and re-evaluate their use.

An attempt has been made by the Commercial List Users’ Committee (the “Committee”) and the Sub-Committee for Standard Form Template Orders (the “Sub-Committee”), to address some of these issues, and to standardize the form of receivership orders. The Sub-Committee has recently finalized the Standard Form Template Receivership Order (the “Model Order”) and the Explanatory Notes to the Model Order (the “Explanatory Notes”).² As a result of the new legal environment the Model Order does not provide many of the powers and protections that insolvency practitioners have come to expect.

THE RISE OF RECEIVER’S POWERS

Although the court appointment of a receiver is currently the favoured approach for maximizing the realization of a debtor’s assets, this was not always the case. For many years, secured creditors preferred

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the appointment of private receivers pursuant to the contractual terms contained in the applicable security agreements. It was thought that private receivers presented the quickest and most cost-effective route to realize on security, particularly with respect to liquidations of all or substantially all of a debtor's assets.

In 1992, s. 244(1) of the BIA was introduced. This section added a minimum ten-day notice period before secured parties could seek to realize on their security in respect of all or substantially all of the assets of a defaulting debtor. In order to protect the secured creditor from having the assets of the debtor dissipated during the notice period, s. 47 was added to allow creditors the right to appoint an interim receiver over the assets of the debtor during this period. At the same time, s. 47.1 was added to allow for the appointment of an interim receiver over the assets of a debtor who had filed a notice of intention or proposal.

Initially, there was the view that ss. 47 and 47.1 interim receivers were intended to be used in the same relatively narrow "watchdog" role that traditional s. 46 interim receivers had played — preventing possible abuse by fraudulent debtors. However, instead of mirroring the language of s. 46, Parliament chose to include broad discretionary language in ss. 47 and 47.1 that authorized the court to direct an interim receiver appointed under these sections to:

(b) exercise such control over the debtor's property, and over the debtor's business, as the court considers advisable; and

(c) take such other action as the court considers advisable.

This language opened the door to appointments which went well beyond the scope of a s. 46 interim receiver.

The issue of these expanded powers was first addressed in 1994 in *Canada (Minister of Indian Affairs & Northern Development) v. Curragh Inc.*³ In *Curragh*, Justice Farley distinguished between a s. 46 interim receiver and a s. 47 interim receiver, noting that s. 47 confers broad powers to deal with the debtor's property and that those powers go far beyond a s. 46 interim receiver's role in preserving property, allowing a s. 47 interim receiver to function as a quasi-receiver and manager/trustee in bankruptcy. Commenting that the interim receivership had continued for a much longer period of time than the ten days as set out in s. 244 of the BIA, Farley J. wrote:⁴

Certainly under these circumstances, the interim receivership has survived for a much longer period of time than the 10 days. It would seem that in many practical aspects in these circumstances that the IR is functioning as a quasi-receiver and manager/trustee in bankruptcy. It would not be generally said that interim receivers have "sale powers" — beyond of course the aspect of disposing of perishable goods or those items with a predilection to depreciation in value. These aspects are referred to in s. 46(2); it would not seem reasonable to assume that a s. 47(1) interim receiver had less authority in this regard. ... [T]he environmental legislation regime appears to have frozen the situation with the likelihood that the [interim receiver] will "continue" until the Faro mine is in fact sold. It appears that the object of the process at the present time is to maintain the property on a shoestring (which has thus far worked) while marketing it with a view towards its sale.

Justice Farley, in noting that the power in the basket clause of s. 47(2)(c), unlike the bulk of the BIA, is not a detailed code, made the often-quoted statement that "...the Court could enlist the services of an interim receiver to do not only what 'justice dictates' but also what 'practicality demands'".⁵

Over the past ten years the powers granted by receivership orders have expanded to the point where most such orders sought in Ontario included not only the power to market and sell assets,⁶ but also:

- a broad stay of proceedings against all third parties;⁷
- protection from environmental liability;
- protection from the obligations of a successor employer;
- exemption from the provisions of the *Bulk Sales Act*;⁸
- a general limitation on the liability of the interim receiver to the proceeds of the estate, except in cases of fraud or gross negligence;
- a provision granting the interim receiver a first charge for its fees;
- the power to terminate contracts;
- the power to assign the debtor into bankruptcy; and
- the power to obtain a first charge for additional financing.⁹

Due to the incredibly broad scope of powers that interim receivers have been able to obtain, they have become one of the most popular realization tools available to insolvency practitioners.

Generally speaking, an interim receiver's powers are granted on a permissive, not mandatory, basis.¹⁰ Usually the section that sets out the interim receiver's powers will have language stating that the interim receiver is "hereby empowered and authorized, but not obligated, ...to do any of the following where the Receiver considers it necessary or desirable...".¹¹ In addition, these receivership orders usually contain a "comeback" clause that allows affected third parties to apply to the court to vary the provisions of the order, but normally only on seven days' notice. This seven-day notice requirement however is normally honoured in the breach.

Although the BIA addresses a number of the powers granted by these orders,¹² the powers granted go far beyond anything expressly provided for in the BIA. Due to the incredibly broad scope of powers that interim receivers have been able to obtain, they have become one of the most popular realization tools available to insolvency practitioners.

THE COURT'S MOVE TO RESTRICT RECEIVERSHIP ORDERS

The mix of broad, potentially unnecessary powers and the *ex parte* nature of the orders granting these powers¹³ have made some courts question both the need for such orders and the courts' authority to grant them. In *Re Big Sky Living*,¹⁴ Justice Slatter took issue with an *ex parte* interim receivership order and raised questions as to what was truly necessary for the protection of the estate or the creditor. Justice Slatter objected to the breadth of the order and its forward-looking approach.

The Order... is in many respects prospective, and it goes far beyond the provisions of the [BIA]. It gives the interim receiver the power to deal with matters that have not arisen, and in all likelihood will never arise.¹⁵

Although Slatter J. recognized the value in not bringing the interim receiver back to court for continuous advice and directions on small points, he was concerned about the effect of a broadly drafted *ex parte* order on third parties such as employees, unsecured creditors, government agencies, landlords and others. He also found several provisions to be "legislative" in nature, in the sense that they purported to provide the receiver with immunity from compliance

with statutory requirements. Among other things, Slatter J. held that the following provisions in the draft order were inappropriate and should not be granted on an *ex parte* basis:

- a provision directing the debtor's legal counsel to deliver documents to the interim receiver on the basis that such provision contravened the debtor's solicitor-client privilege;
- a provision exempting the interim receiver from compliance from the notice requirements of the (Alberta) *Personal Property Security Act* prior to the sale of the debtor's assets;
- a provision authorizing the interim receiver to assign the debtor into bankruptcy and to act as trustee in bankruptcy;
- a provision restraining contracting parties from terminating, ceasing to perform or altering contracts with the debtor;
- a provision declaring employees of the debtor to be automatically dismissed upon the making of the order and stipulating that the interim receiver would not be a successor employer; and
- a provision limiting the liability of the interim receiver to the net realizable value of the debtor's assets.

Moreover, Feldman J.A. found that Ground J. did not have jurisdiction to order that the interim receiver — even acting only as qua realizor — was not a successor employer since determination of that issue lay within the exclusive jurisdiction of the OLRB.

The argument that Ontario courts routinely granted orders containing the above provisions was not persuasive, nor was the argument that commercial realities necessitated the granting of broad powers to the interim receiver in the initial application. Justice Slatter found that the "comeback" clause in the order was not a complete answer to the issues he raised with respect to the "sweeping provisions" of the order. He resisted the shifting of the burden of proof from the interim receiver to affected parties on the basis that affected parties were prejudiced because of the need to obtain leave of a court to do things that were not otherwise prohibited and because of the expense imposed upon third parties to seek such relief.

Although Ontario courts continue to grant very broad receivership orders, there are signs that the tide may be turning. In *GMAC Commercial Credit Corp. of Canada v. T.C.T. Logistics Inc.*,¹⁶ the issue of whether the bankruptcy court had the authority under the BIA to effectively immunize an interim receiver

from obligations as a successor employer was addressed. At first instance, Justice Ground, amended the original appointment order such that it would only protect the interim receiver where it acted *qua* realizor. Justice Ground then denied the union leave to bring a successor employer proceeding before the Ontario Labour Relations Board (the "OLRB") finding that the interim receiver had, in fact, only acted *qua* realizor and not *qua* employer.

The union appealed and Justice Feldman, writing for the majority, analyzed various sections of the BIA in order to find a statutory source for a judge to grant the order sought. She first looked at s. 47, finding that the broad language in the basket clause in s. 47(2) did not provide support for trumping rights created under provincial statutes. Moreover, Feldman J.A. found that Ground J. did not have jurisdiction to order that the interim receiver — even acting only as *qua* realizor — was not a successor employer since determination of that issue lay within the exclusive jurisdiction of the OLRB.

Counsel for the receiver argued that failing to grant interim receivers protection from the OLRB in circumstances where they operate a business would force them to wind up a business and liquidate the assets even if this would not provide an optimal outcome for stakeholders. This was due to the fact that interim receivers (and the secured creditors who typically indemnify them) would not want to be exposed to personal liability for costly employee obligations. In response to this Feldman J.A. stated:¹⁷

I do not know what receivers will do in the future. However, the uncertainty and potential for increased costs are clear and will necessarily affect the practice of appointing receivers and the decisions of creditors as to how they will proceed, and could affect the willingness of a receiver or trustee to act. Where a creditor is funding the receivership, any personal liability imposed on the receiver for complying with a collective agreement will be factored in as an additional cost of the receivership....

Justice Feldman went on to consider whether the stay should be lifted to permit the unions to apply to the OLRB for a determination that the receiver was a

successor employer. This required a review of s. 215 of the BIA, which provides that a person who wishes to commence proceedings against an interim receiver must obtain leave of the court. Justice Feldman found that the low threshold previously used for granting leave under s. 215 was inappropriate with respect to successor employer liability¹⁸ and noted that "...it is both necessary and appropriate that the bankruptcy court use its power under s. 215... to assist the receiver in achieving the best financial result for creditors and employees of the debtor, in most cases, by operating the business in order to sell it as a going concern".¹⁹ She concluded that s. 215 could be used by the court to protect an interim receiver from the scrutiny of the OLRB in certain circumstances and set the matter back to be heard by the Commercial List.²⁰ In deciding whether the stay should be lifted, Feldman J.A. indicated that the following factors should be considered by the court.²¹

Finally, and possibly most importantly, Feldman J.A. affirmed the judgment in Big Sky in that she stated that the practice of interim receivers obtaining ex parte appointment orders that grant them extensive powers as well as immunity from responsibilities to third parties not before the court should no longer be sanctioned in Ontario.

...the timing of the application, the complexity of the receivership and the demands on the receiver as it carries out its obligations, the potential duration of the period that the receiver intends to operate the business before it can be sold (normally as brief as possible), the availability of potential purchasers and their financial strength, and the likelihood that a purchaser will be declared a successor employer and assume all of the obligations under the collective agreement. This latter factor may be particularly important because it will give practical assurance to the union that all of the terms of the collective agreement will be honoured and the employees protected. Another key factor is the practicality of proceeding before the OLRB and the timeliness of a hearing before that tribunal in the context of the proposed temporary operation of the business and its sale.

Finally, and possibly most importantly, Feldman J.A. affirmed the judgment in *Big Sky* in that she stated that the practice of interim receivers obtaining *ex parte* appointment orders that grant them extensive powers as well as immunity from responsibilities to third parties not before the court should no longer be sanctioned in Ontario.²²

As a result, it would appear that interim receivers can no longer be shielded from successor employer

liability by including immunity language in *ex parte* receivership orders. Furthermore, to the extent that other affected third parties have statutory rights that they may wish to enforce under provincial law, such as certain environmental regulations, *ex parte* orders that grant broad powers or immunities to interim receivers may not be granted.

It remains to be seen whether the *T.C.T. Logistics* decision will have broader application and result in Ontario courts refusing to grant orders that restrict rights of other third parties that have not been given notice — such as landlords and persons having contracts with the debtor. The Model Order (discussed below), however, would suggest that the impact of *T.C.T. Logistics*, at least for now, may be limited to attempts to immunize the receiver from statutory obligations.

THE MODEL ORDER

In 2003, the Sub-Committee commenced the task of developing the Model Order. The Sub-Committee is comprised of insolvency lawyers and the Model Order was drafted in consultation with various government departments,²³ members of the judiciary²⁴ and professional organizations.²⁵

In the Explanatory Notes,²⁶ the Sub-Committee has indicated that the Model Order is meant to be a starting point and not a ridged template from which one cannot deviate. As each insolvency is unique, the provisions of the Model Order will need to be restricted and/or expanded to apply to the specific situation at hand. The Model Order does not seek to resolve any legal issues or to prevent counsel from seeking to include any provisions that appear advisable in any given case, but the Sub-Committee has requested that if counsel choose to adopt provisions that depart from the Model Order, they should bring these changes to the attention of the court.²⁷

PRELIMINARY MATTERS

There are a number of different types of Court Officers (trustees, receivers, managers, receiver-managers, interim receivers, etc.) to choose from when seeking an appointment to realize on a debtor's assets. In Ontario, most receivership orders have in-

cluded the appointment of both an interim receiver under s. 47(1) or 47.1 of the BIA and a receiver and manager under s. 101 of the *Courts of Justice Act*.²⁸ The Model Order follows this approach as:²⁹

1. An order appointing an Interim Receiver under the BIA has national scope and is readily enforceable nationally (subject always to local concerns as often may arise in Quebec and elsewhere);
2. An interim receiver bases its jurisdiction federally and may be better protected against certain provincial liabilities and certain inequities that may flow from the application of different provincial regimes to the same debtor's property as may be located in different provinces;
3. A receiver and manager under the CJA can be provided with a priming charge in respect of its disbursements and thereby avoid the limits on the authority of the Court to grant a priming charge in respect of business losses suffered by an Interim Receiver [under s. 47.2 of the BIA].

The Sub-Committee also noted that use of both the BIA and CJA avoids any concern that the use of an interim receiver — who technically does not fall within the definition of “receiver” found in s. 243(2) unless it takes possession and control of the debtor's assets — may be used to frustrate the statutory rights of suppliers under s. 81.1 of the BIA in respect of 30-day goods.

Although not noted in the Explanatory Notes, a further reason for using both the CJA and BIA may turn on appeal rights. Under s. 135 of the BIA, it would appear that an interim receivership order would be automatically stayed upon the filing of an appeal — which in most cases would require the secured creditor to bring an emergency motion to lift the stay. The reverse is true under the CJA where a receivership order would not be stayed by the filing of an appeal. Thus, it is possible that if a receivership order filed under both the BIA and the CJA is appealed, the secured creditor could rely on the CJA appointment even though the BIA appointment is stayed.

The Model Order also provides for the listing of parties served and the appearance or non-appearance of those parties on the motion as opposed to the general language of “on hearing submissions of counsel present”, as appeal rights, effective vesting and even the effectiveness of the receivership order may depend upon proof of service and appearance.

THE RECEIVER'S POWERS

The powers that are specifically enumerated in the Model Order include the standard powers to take possession of, and preserve, the debtor's property. The Model Order also gives the receiver the power to manage the business, hire consultants as required, enter into transactions, compromise claims owing to the debtor, proceed with litigation and market and sell assets, subject to the prior approval of the court in the case of sales exceeding a materiality level to be specified.

The Explanatory Notes state that it is expected that, as an officer of the court, the receiver will engage in meaningful communications with and, be accountable to, all stakeholders and not just the secured creditor. This is reflected in subpara. 3(c) of the Model Order.

The Model Order does not contain a specific provision allowing the receiver to file an assignment in bankruptcy or to consent to the making of a receiving order as the Sub-Committee felt that bankruptcy was a

sufficiently material, substantive and final act that the matter should be brought to the attention of the court expressly at the appropriate time.

INJUNCTIONS, POSSESSION, AND ACCESS TO PROPERTY

As receivers generally need the co-operation of third parties, receivership orders normally have broad injunctions against non-parties that are designed to ensure compliance and co-operation with the receiver. The Model Order requires everyone with notice of the order to advise the receiver of the existence of any of the debtor's property in their possession or control and to deliver to the receiver such of the debtor's property as the receiver requires. The Explanatory Notes state that the Sub-Committee believes that lim-

The Model Order does not contain a specific provision allowing the receiver to file an assignment in bankruptcy or to consent to the making of a receiving order as the Sub-Committee felt that bankruptcy was a sufficiently material, substantive and final act that the matter should be brought to the attention of the court expressly at the appropriate time.

iting the obligation to deliver up the debtor's property to only those cases where the receiver requires the property will save costs for the third parties and protect the estate from being forced to incur costs to move or store unnecessary property. The Model Order addresses the issue of solicitor-client privilege raised in *Re Big Sky Living* and exempts records that may not be disclosed due to solicitor-client privilege or statutory provisions prohibiting disclosure.

THE STAY OF PROCEEDINGS

The Model Order provides specific stay-related relief, but attempts to clean up some of the over inclusive and repetitive language found in many receivership orders. The following five heads of relief are provided in the Model Order:

- a stay of proceedings against the receiver;³⁰
- a stay of proceedings against the debtor;
- a stay of the exercising of any rights or remedies against the debtor;
- a stay of third party contractual termination rights; and
- a stay requiring third parties to continue to supply goods and/or services.

The Model Order does not include a broad provision that would order counter-parties to renew contracts with the debtor. Instead, third parties are restricted only from failing to "honour renewal rights". To the extent that anyone wishes to seek to force a renewal in the absence of a contractual renewal right, the relevant provision in the order would have to be brought to the attention of the court in which case the court may insist that notice be provided to the affected parties.

The Explanatory Notes state that the government representatives who made representations to the Sub-Committee submitted that the stay of proceedings should not operate to prevent regular enforcement of day-to-day regulatory requirements affecting the debtor's business. Although the Sub-Committee did not agree that government agencies should be entirely exempt from the stay provisions, an exception was

built into the Model Order³¹ so that the receiver is not exempt from obligations to comply with statutory and regulatory provisions relating to health, safety or the environment.

ENVIRONMENTAL ISSUES

An important consideration in any receivership is assessing the nature and extent of any environmental liability. Receivers have been chosen as the appropriate realization vehicle numerous times where there was a concern that taking possession of property with potential environmental contamination could result in personal liability for the costs associated with any clean up.

Following the decisions in *Big Sky* and *T.C.T. Logistics*, the Model Order has stripped out provisions that would purport to immunize the receiver against a finding that it has occupied, possessed or taken control of a property. The Model Order provides that the receiver is not required by the order to "occupy or take control, care, charge, possession or management (separately and/or collectively, "Possession") of any property that might be environmentally contaminated...". Accordingly, the receiver can only incur liability for environmental harm that occurs after its appointment when it in fact takes possession of environmentally contaminated property.

Section 14.06(2) of the BIA provides some protection to receivers from personal liability in respect of environmental conditions or damage that occurred before their appointment and

after their appointment unless the condition arose or damage occurred on account of the receiver's gross negligence or wilful misconduct. However, to the extent that a receiver exercises its powers or does in fact take possession of the contaminated property, it should obviously investigate whether such actions will cause it to incur any liability with respect to the property in question.

EMPLOYMENT ISSUES

Counsel have historically taken measures in receivership orders to ensure that receivers are protected

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