# Restructuring and Insolvency in Canada: Overview

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Country Q&A | Law stated as at 01-Jun-2025 | Canada

A Q&A guide to restructuring and insolvency law in Canada.

The Q&A gives a high level overview of the most common forms of security granted over real and personal property; creditors' and shareholders' ranking on a company's insolvency; mechanisms to secure unpaid debts; mandatory set-off of mutual debts on insolvency; state support for distressed businesses; rescue and insolvency procedures; stakeholders' roles; liability for an insolvent company's debts; setting aside an insolvent company's pre-insolvency transactions; carrying on business during insolvency; additional finance; and multinational cases.

## Forms of Security

1. What are the most common forms of security granted over immovable and movable property? What formalities must the security documents, the secured creditor or the debtor comply with? What is the effect of non-compliance with these formalities?

### Immovable Property (Real Property)

**Common forms of security and formalities.** Real property security interests are governed by provincial mortgage, title, and lending statutes, which regulate both the registration requirements and enforcement processes for real property security interests. Real property security is commonly granted through either a mortgage or a debenture.

Mortgages, the most common instrument through which a borrower grants a security interest in real property to a secured party, are governed by each of the Canadian provinces and territories' land title statutes. Under these statutes, the general key requirements for establishing a valid and enforceable charge on real property are that the mortgage must:

- Properly identify the parties to the mortgage.
- Secure an underlying debt obligation.
- Contain charging language creating a security interest for the benefit of a secured party.
- Contain a proper legal description of the real property.

 

A secured party can also use a debenture to create a security interest over real property, which creates a promise to pay, a charge over the real property, and a floating charge over all the real and personal property of the borrower. To create a charge over a borrower's real property, a debenture generally must contain the same fundamental elements as a mortgage.

**Effects of non-compliance.** Non-compliance with the applicable registration requirements for real property renders the secured party's security interest unenforceable. As a result, the creditor will rank *pari passu* (on equal footing) with other unsecured creditors.

### Movable Property (Personal Property)

**Common forms of security and formalities.** In Canada's common law provinces and territories, the granting of security interests in personal property (outside a formal restructuring or insolvency process) is governed by each jurisdiction's *Personal Property Security Act* (PPSA). This contrasts with Québec, which operates under a civil law system where security interests in movable property are governed by the *Civil Code of Québec*. Security interests in Québec are outside the scope of this guide.

The creation of security interests under the PPSA regimes is a matter of substance over form. Any binding agreement, whether oral or written, that has the effect of granting a security interest in personal property is considered a security agreement. For a security interest to be enforceable, the security interest must be:

- Attached to the collateral.
- *Perfected*.

To achieve attachment:

- There must be a security agreement containing a description sufficient to identify the collateral.
- The secured party must give value to the debtor.
- The debtor must have rights in the collateral.

For perfection to occur:

- The security interest must have attached.
- Depending on the nature of the collateral, the secured party must have either effected a registration under the applicable Personal Property Security Registry (PPSR) or have taken possession or control of the collateral for the purposes of perfection.

With respect to the priorities of multiple perfected security interests, the first security interest registered under the PPSR typically prevails, although there are exceptions to this, including, among others, special priority rules related to *purchase-money security interests* (PMSI) in certain types of collateral.

**Effects of non-compliance.** Failure to perfect a security interest may result in a security interest ranking behind in priority to other secured creditors. A creditor with a perfected security interest will have priority over a secured creditor that has not perfected its security interest (section 20(1), Ontario's PPSA, R.S.O. 1990, c. P.10).

## Creditor and Contributory Ranking

 

2. Where do creditors and contributories rank on a debtor's insolvency?

The *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (BIA) codifies the ranking of claims in a bankruptcy. The BIA's priority scheme is expressly subject to the rights of secured creditors, enabling secured creditors to enforce against their collateral for payment of their respective claims. The priority as among secured creditors is determined according to provincial statutes governing the creation, maintenance, and enforcement of security interests, along with the *Bank Act*, S.C. 1991, c.46.

Claims in a bankruptcy are generally ranked in priority as follows:

- Claims by owners of property held in the possession of the bankrupt, for example, property held in trust.
- Claims given "super priority" status under the BIA, including:
  - costs of environmental remediation incurred by federal or provincial governments;
  - claims made by suppliers for the return of goods supplied to the debtor within the 30-day period before bankruptcy;
  - government statutory deemed trusts for source deductions (that is, payroll reductions, Canada Pension Plan deductions, and unemployment insurance deductions); and
  - claims for up to CAD2,000 for unpaid salary, wages, commissions, and benefits.
- Claims of preferred creditors, as described and prioritised under the BIA, including the trustee's administrative expenses and legal fees.
- All other unsecured claims.

Under-secured creditors can submit a claim as an unsecured creditor for the balance of their claim, and preferred creditors can also file unsecured claims for any portion of their claim limited in the priority scheme outlined above. Unsecured creditors are paid on a pro rata basis. The BIA subordinates other claims to rank below general unsecured claims, with equity claims being the lowest in priority.

Under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (CCAA), any court-ordered charges that have been granted are typically afforded super priority status, including charges in favour of a *debtor-in-possession* (DIP) lender (see *Question 12*), directors of a debtor company, professional advisors, critical suppliers, or a key employee retention plan.

## Unpaid Debts and Recovery

 

3.Can trade creditors use any mechanisms to secure unpaid debts? Are there any legal or practical limits on the operation of these mechanisms?

In specific circumstances, a debt owed to a trade creditor can be secured by registering a PMSI. A PMSI is a form of security interest that arises when a creditor finances or supplies a specific good to a debtor on credit, which has special priority under the Ontario PPSA. Provided that the PMSI complies with the technical notice and registration requirements, it will have priority over other security interests over the same goods.

In a bankruptcy or BIA proposal proceeding, an unpaid supplier may be entitled to repossess unpaid goods if the following conditions are met:

- The supplier provides a written demand of repossession within 15 days of the debtor's bankruptcy.
- The goods were delivered within 30 days before the debtor's bankruptcy.
- The goods are in possession of the purchaser, trustee, or receiver.
- At the time the demand is issued, the goods:
    - are in the possession of the purchaser, trustee, or receiver;
    - are identifiable as the goods delivered by the supplier;
    - are in the same state as they were on delivery;
    - have not been resold at arms' length; and
    - are not subject to any agreement for sale at arms' length.
- The purchaser, trustee, or receiver does not, forthwith after the demand is presented, pay to the supplier the entire balance owing (section 81.1(1), BIA).

In a CCAA proceeding, a court may issue an order declaring a person as a critical supplier of the debtor company, requiring continued supply of goods or services. In these circumstances, the court will grant the supplier a charge over the debtor's property to secure payment in an amount equal to the value of the goods or services supplied pursuant to the order (section 11.4, CCAA).

4. Can creditors invoke any procedures (other than the formal rescue or insolvency procedures described in *Question 6* and *Question 7*) to recover their debt? Is there a mandatory set-off of mutual debts on insolvency?

Together with the formal restructuring and insolvency proceedings (see *Question 6* and *Question 7*), out-of-court (or informal) restructurings are permitted in Canada and are commonly completed against the backdrop of potential court-supervised proceedings. The ability of a debtor to implement an out-of-court restructuring often depends on the complexity of the debtor's capital structure. Out-of-court restructurings frequently involve forbearance agreements and implementation of some pre-emptive transaction, such as:

- An equity injection or equity exchange.
- A non-core asset sale.
- New or refinanced debt.

In PPSA jurisdictions, a secured creditor can exercise self-help remedies, including taking possession of collateral. A secured creditor who has taken possession of collateral generally has the right, on complying with certain notice provisions, to either:

- Sell the collateral through a commercially reasonable private or public sale to recover the outstanding debt.
- Foreclose and take the collateral in full satisfaction of the outstanding debt.

If the debtor or another party with an interest in the collateral objects to the foreclosure, the secured creditor must sell the collateral. Exercising a foreclosure remedy eliminates the outstanding debt and bars a secured creditor from suing for the deficiency, while a sale process preserves this right.

In formal restructuring and insolvency proceedings, the CCAA and the BIA both expressly preserve the right of set-off. Courts have clarified that set-off generally only applies between pre-filing claims (with some exceptions). While set-off between pre- and post-filing claims is stayed, in *Montréal (Ville) c. Restructuration Deloitte Inc.*, 2021 SCC 13, a majority of the Supreme Court of Canada held that courts may lift the stay to allow for set-off in exceptional circumstances.

## State Support

5. Is state support for distressed businesses available?

Canadian federal and provincial governments typically do not provide financial support for financially distressed business subject to unique circumstances. For example, during the COVID-19 pandemic, temporary measures were introduced by the federal and provincial governments, including subsidy initiatives to temporarily support wage and rent expenses and grants aimed at supporting small businesses.

In addition, the federal Wage Earners Protection Program provides compensation to employees who are owed wages, vacation pay, termination pay, or severance pay when their employer becomes bankrupt or subject to a receivership.

## Rescue and Insolvency Procedures

6. What are the main rescue/reorganisation procedures in your jurisdiction?

## CBCA Plans of Arrangement

**Objective.** The primary objective of a plan of *arrangement* under the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44 (CBCA) is to facilitate the reorganisation of a corporation incorporated under the CBCA, including the restructuring of its debt obligations, through a corporate arrangement, without requiring a declaration of insolvency. CBCA plans are a unique process that are attractive to highly leveraged companies with complex capital structures. The CBCA does not generally provide for the restructuring of trade debt, employee obligations, or other obligations or claims of this nature.

**Initiation.** A formal CBCA plan process begins when an applicant company, which must be a CBCA corporation, files an ex parte motion to obtain an interim order from the court. The interim order authorises the company to call and conduct meetings with affected security holders to vote on the proposed CBCA plan. However, before seeking an interim order, companies typically engage with key stakeholders. This often culminates in a support agreement, in which the key stakeholders agree to support, and vote in favour of, the proposed CBCA plan.

**Substantive tests.** To proceed with a CBCA plan, three statutory requirements must be met:

- The proposed transaction must qualify as an arrangement as defined under the CBCA. The definition of “arrangement” under the CBCA includes the exchange of securities of a corporation (for example, any equity security or debt obligation) for property, money, or other securities of the corporation or of another body corporate.
- The applicant must not be insolvent. To meet this requirement, a new company applicant can merge with the debtor (which can be insolvent) as part of the plan of arrangement. The solvency requirement has also been found to be satisfied where two insolvent corporations merge or enter into a transaction or transactions, which results in the emergence of a single solvent restructured entity.
- It must not be practical to effect the desired change under another provision of the CBCA, ensuring that the arrangement process is used only when there are no other viable mechanisms under the CBCA for implementing the proposed transaction.

In addition to these requirements, when making a final order the court must be satisfied that the plan of arrangement is fair and reasonable, and that the application has been put forward in good faith.

**Consent and approvals.** While there is no statutory requirement for stakeholder approval, courts typically require approval by at least 66.67% of the total value of claims for each class of affected stakeholders voting on the plan. Shareholder approval is usually not required. The appropriate level and type of stakeholder approval is a matter of judicial discretion. Following stakeholder approval, the debtor must seek a final court order approving the plan of arrangement to make it legally binding on all affected stakeholders.

**Supervision and control.** Management retains control of the business in a CBCA reorganisation. There is no supervisory officer similar to a CCAA monitor or a BIA proposal trustee.

**Protection from creditors.** As part of implementing a CBCA plan of arrangement, the corporation can seek court-ordered releases and waivers in respect of matters relating to the proceedings, transaction, and affected securities.

 

**Length of procedure.** A CBCA plan of arrangement can be implemented in 60 to 90 days, although a pre-packaged CBCA restructuring can be completed in a shorter time frame (about 30 to 45 days).

**Conclusion.** Once a final order from the court is obtained, the applicants can implement the CBCA plan, which legally binds all stakeholders, including stakeholders who are part of an affected class that did not vote in favour of the plan.

For further information, see *Plan of Arrangement Toolkit*.

## CCAA Proceedings

**Objective.** The CCAA is a flexible statute with a broad remedial purpose. The main objective of the CCAA is to facilitate compromises and arrangements between insolvent companies and their creditors to avoid the economic and social consequences of liquidation. CCAA proceedings are typically employed to achieve one of three outcomes:

- To enable an insolvent company to formulate a CCAA plan of arrangement with respect to the company's obligations to its creditors.
- To implement a sales process, or pre-packaged sale transaction.
- To facilitate an orderly wind-down of the debtor company.

**Initiation.** CCAA proceedings begin with an application by the debtor company or, less commonly, a creditor, and the issuance of a court order declaring, among other things, that the debtor is a company to which the CCAA applies. In contrast to other restructuring procedures, such as a BIA proposal, a CCAA proceeding requires an application to the court to obtain a stay of proceedings.

The CCAA defines a company as "any company, corporation, or legal person incorporated by or under an Act of Parliament or of the legislature of a province and any incorporated company having assets or doing business in Canada, wherever incorporated and any income trust" (section 2(1), CCAA). The definition of a company expressly excludes:

- Banks.
- Foreign banks as defined in section 2 of the *Bank Act*.
- Telegraph companies.
- Insurance companies.
- Companies to which the *Trust and Loan Companies Act*, S.C. 1991, c. 45 applies.

Directors of an insolvent corporation are not obligated to initiate rescue or reorganisation procedures on behalf of an insolvent corporation. However, directors should be cautious while operating in financial distress as they may risk facing liability, including for gross negligence, wilful misconduct, or through an oppression claim from creditors or other stakeholders if a company continues to operate while insolvent. Directors may also be personally liable for certain liabilities of the company (see *Question 9*).

**Substantive tests.** A CCAA proceeding can be initiated by a debtor company (section 2(1) "debtor company," CCAA) or a group of affiliated companies that:

- Have assets in Canada (or carries on business in Canada).

 

- Have total liabilities in excess of CAD5 million.
- Are insolvent, bankrupt, or have committed an "act of bankruptcy" (section 42(1), BIA).

Courts have interpreted the term "insolvent" broadly under the CCAA and have accepted that a debtor company will be insolvent if there is a reasonably foreseeable liquidity crisis.

**Consent and approvals.** A CCAA proceeding is commenced on the issuance of an order (referred to as an Initial Order) that, among other things, declares the debtor is a company to which the CCAA applies and provides a stay of proceedings. The relief granted in an Initial Order must be limited to what is reasonably necessary.

The debtor applicant can give little or no notice of the initial hearing to prevent a race to enforce defaults before the Initial Order being made. The initial hearing is brought in the province of the debtor's head office or chief place of business.

If a CCAA plan of arrangement is being presented by the insolvent company, the plan must be approved by a double majority of creditors in each class of creditors voting on the plan which is:

- 50% plus one of the total number of creditors voting in the class.
- 66.67% of the total value of claims of voting creditors.

**Supervision and control.** An Initial Order must appoint a "monitor" as a court-officer to supervise and report on the debtor company's activities, liaise with creditors, and assist in the debtor company's restructuring efforts. The debtor company generally retains control and possession of its assets and continues to operate its business during a CCAA proceeding (see *Question 11*).

An Initial Order also typically provides approval for DIP financing (see *Question 12*). The amount of DIP financing that a court can approve on an initial CCAA application is limited to what is reasonably necessary for the continued operation of the debtor in the ordinary course of business during the initial ten-day stay period. However, this amount is typically increased at the subsequent comeback hearing.

**Protection from creditors.** The CCAA permits the court to order a stay of proceedings that will be imposed against, among others, all creditors (secured and unsecured), landlords, and persons who are not creditors of the debtor company, to prevent them from exercising contractual rights that would make it difficult, if not impossible, for the debtor company to proceed with its reorganisation.

Given that the debtor company usually brings the initial application in a CCAA proceeding without notice to other parties, the initial stay period is intended to ensure that parties affected by the CCAA proceedings have notice and an opportunity to address the court early in the proceedings. The length of a stay of proceedings under the Initial Order is limited to ten days. The stay of proceedings can be repeatedly extended at the discretion of the court for further periods as the court deems appropriate (typically in 60 to 90-day intervals).

The CCAA prohibits contractual counterparties from terminating, amending, or claiming an accelerated payment or forfeiture of the term under an agreement with a debtor company by reason only that the debtor has commenced CCAA proceedings or has become insolvent. However, suppliers (including landlords) are entitled to require immediate payment for goods or services (including rent) supplied to the debtor post-filing.

**Length of procedure.** CCAA proceedings can take several months to years, although a pre-packaged CCAA restructuring can be completed in a short time frame (several weeks).

**Conclusion.** Given the flexibility of the CCAA, a CCAA proceeding can conclude in numerous ways, including the emergence of the debtor company as a single solvent restructured entity, the sale of certain assets of the debtor company, or the sale of the debtor company as a going concern.

For further information, see *Practice Note, CCAA Reorganizations: Overview*.

## BIA Commercial Proposals

**Objective.** The primary objective of a BIA proposal is to enable an insolvent company to avoid bankruptcy through submitting a proposal to its creditors, which may involve reducing the aggregate debt owed, extending the repayment period, or both. Compared to CCAA proceedings, the BIA proposal process is more rigid and rule-driven, making it less suitable for complex restructurings.

**Initiation.** A BIA proposal can only be commenced by an "insolvent person" or a person acting on their behalf. A creditor is not permitted to commence a BIA proposal process.

A BIA proposal is initiated by filing either a proposal or a notice of intention to file a proposal (NOI). An NOI is a one-page statement signed by the debtor and filed with the Official Receiver (the federal government appointee responsible for administering the BIA). The NOI must include the consent of a trustee in bankruptcy who has agreed to act as trustee under the proposal and a list of all creditors with claims exceeding CAD250. The debtor, within ten days after filing the NOI, must file a cash-flow statement with the Official Receiver, which must also be verified by the trustee. After filing a NOI, the debtor has 30 days to file a proposal with the Official Receiver.

**Substantive tests.** Section 2 of BIA defines an "insolvent person" as an individual, corporation, partnership, or unincorporated association which:

- Is not bankrupt.
- Carries on business, resides, or has property in Canada.
- Has liabilities that equal or exceed CAD1,000.
- Is insolvent by virtue of:
  - an inability to meet their obligations as they become due;
  - having ceased to pay their current obligations in the ordinary course as they become due; or
  - having property with an aggregate value that is insufficient, or, if disposed of, would not be sufficient to enable payment of all of their obligations due and accruing due.

**Consent and approvals.** Once a proposal is filed with the Official Receiver, the trustee must hold a meeting of creditors to approve the proposal and the court must approve the proposal.

A proposal can be made to creditors generally or to classes of creditors (both secured and unsecured) whom the debtor wishes to compromise. A proposal must be approved by a double majority of creditors in each class of creditors voting on the proposal which is:

 

- 50% plus one of the total number of creditors voting in the class.
- 66.67% of the total value of claims of voting creditors.

A proposal made to a class of secured creditors that is not approved by that secured creditor class cannot affect the rights of those secured creditors but can still become effective against unsecured creditors, provided that it is passed by the class or classes of unsecured creditors voting on the proposal.

Shareholders are only given a right to vote on a BIA proposal if it is expressly ordered by the court.

**Supervision and control.** During a BIA proposal proceeding, the debtor company remains in possession and control of their assets and business but must name a licensed insolvency trustee to act as a trustee under the proposal. The trustee has legislatively mandated duties and responsibilities in respect of the debtor and the proposal itself, including helping prepare financial information related to the debtor and reporting to the court and creditors.

BIA proposals are also a court-supervised process. Court approval is needed for most key steps in a BIA restructuring.

**Protection from creditors.** A stay of proceedings automatically arises under the BIA on the filing of a proposal or a NOI and binds all secured and unsecured creditors. The stay of proceedings operates throughout the period from the date of filing the proposal or NOI to the date of court approval of the proposal. In respect of those debts compromised by the proposal, the stay of proceedings operates beyond that period.

Counterparties are expressly prohibited from terminating, amending, or claiming an accelerated payment or forfeiture of the term under an agreement with a debtor company for the sole reason that the debtor has commenced BIA proceedings or has become insolvent (section 84.2(1), BIA). However, suppliers (including landlords) are entitled to require immediate payment for goods or services (including rent) supplied to the debtor post-filing.

**Length of procedure.** A BIA proposal must be completed within approximately six months of filing a NOI. After filing a NOI, the debtor has 30 days to file a proposal with the Official Receiver. This 30-day period may be extended, on court application, for up to a maximum of five additional months, provided that extensions are to enable the debtor to file its proposal. Extensions can be granted only for periods of up to 45 days at a time. Failure to file a proposal within the 30-day period (as may be extended), or a failure to provide a cash-flow statement (see above, *BIA Commercial Proposals*) will result in the debtor being deemed to have made an assignment in bankruptcy.

**Conclusion.** The debtor company retains control over its assets and business. If the requisite majority of creditors in each class vote in favour of the proposal and it receives court approval, the proposal is implemented. Provided that the debtor company has fulfilled its obligations under the proposal, the debtor company will successfully emerge from the proceedings. Should the debtor company fail to satisfy the obligations outlined in the approved BIA proposal, or if the proposal is rejected by its creditors, the debtor company will be deemed to have assigned itself into bankruptcy.

For further information, see *Practice Note, BIA Proposals: Overview*.

7. What are the main insolvency procedures in your jurisdiction?

 

## Bankruptcy/Liquidation Proceedings

**Objective**. The BIA is the primary statute used to liquidate a debtor company. The objective of a bankruptcy proceeding under the BIA is to enable creditors to pursue a claims process through a collective, orderly, and equitable administration of the bankrupt's assets.

**Initiation.** A debtor company can initiate bankruptcy proceedings under the BIA by filing an assignment for the benefit of its creditors in the prescribed form and a sworn statement of affairs with the Official Receiver. Once the Official Receiver accepts the assignment for filing, the Official Receiver must appoint a licensed insolvency trustee to act as trustee in bankruptcy.

A debtor company can also be involuntarily placed into bankruptcy if either:

- One or more creditors files an application with the court for a bankruptcy order against a debtor.
- The debtor company fails to comply with the obligations outlined in a BIA proposal or fails to obtain creditor approval for its BIA proposal (see *Question 6*, *BIA Commercial Proposals*).

**Substantive tests.** For a debtor company to voluntarily assign itself into bankruptcy, it must establish that it is an "insolvent person" under section 2 of the BIA (see *Question 6*, *BIA Commercial Proposals*).

For a creditor to assign a debtor company into bankruptcy, the creditor must establish that it is owed at least CAD1,000 from the debtor and that the debtor has committed an act of bankruptcy under the BIA (that is, ceasing to meet its liabilities as they generally become due) within the six months before the application.

**Consent and approvals.** Creditor and debtor-initiated bankruptcy proceedings require court approval. A court must be satisfied that all the statutory requirements (see above, *Bankruptcy/Liquidation Proceedings*) have been met before granting a bankruptcy order.

**Supervision and control.** On the issuance of a bankruptcy order or the filing of an assignment in bankruptcy, the assets of the bankrupt immediately vest in the trustee in bankruptcy (who is an officer of the court and has a duty to act in the interests of all creditors). At this point, the debtor cannot deal with its assets and the trustee will proceed to liquidate the assets of the estate and distribute the proceeds in accordance with the BIA priority scheme.

**Protection from creditors.** In a bankruptcy, the debtor's unsecured creditors are prohibited, under an automatic stay of proceedings, from:

- Commencing any proceedings against the debtor to recover their debts.
- Exercising any rights against the debtor or its property.

Because the trustee takes the debtor's assets subject to the rights of secured creditors, secured creditors are not subject to the automatic stay and retain the ability to use private enforcement remedies.

In a bankruptcy, the debtor's existing contracts are not automatically terminated (other than employment contracts). A trustee can perform any of the debtor's existing contracts where it would be necessary or beneficial to the estate administration. Based on the automatic vesting of the debtor's property in the trustee, contractual rights and obligations are statutorily transferred and need not be expressly assumed by the trustee. However, if the trustee does not take affirmative steps to insist on a contract's completion within a reasonable period of time, the contract can be considered terminated.

 

The trustee also has the express right to disclaim any lease, or other temporary interest in the bankrupt's property (section 30(1)(k), BIA), provided that the counterparty can apply to the court to review that disclaimer. The automatic bankruptcy stay provision under the BIA has not been interpreted as to prevent contract counterparties from terminating their agreements with the debtor, and unlike the CCAA and the BIA's proposal regime, there is no separate provision that applies in a bankruptcy to prevent contracting counterparties from terminating their agreements by reason of the debtor's bankruptcy.

**Length of procedure.** The length of a liquidation proceeding depends on several factors such as the nature of the debtor's assets, the number of creditors, and how difficult it is to liquidate the debtor company's assets.

**Conclusion.** Once the trustee in bankruptcy has administered the debtor's estate, the trustee in bankruptcy applies to the court for a discharge. A bankrupt corporation can only be discharged from bankruptcy if it is able to satisfy all its creditors in full.

CCAA proceedings can also be used to facilitate the liquidation of a debtor company. The procedural elements, for example, initiation, substantive tests, required consents and approvals, and the stay of proceedings are generally consistent with those outlined in *Question 6*.

For further information, see *Practice Notes Bankruptcy: Overview*.

## Stakeholders' Roles

8. Which stakeholders have the most significant role in the outcome of a restructuring or insolvency procedure? Can stakeholders or commercial/policy issues influence the outcome of the procedure?

### Stakeholders

Stakeholders of a debtor company can have significant influence on the type of restructuring or insolvency procedure a debtor company utilises. Key stakeholders whose interests may influence the decision-making process for a restructuring path include:

- **Secured creditors**. Secured creditors are typically the most influential stakeholders in a restructuring or insolvency procedure. They possess statutory and, often, contractual rights to appoint a receiver to enforce their security over the debtor's assets and liquidate those assets under a prescribed process, among other rights. Distressed companies often pursue CCAA or BIA restructurings to protect themselves against a receivership application. In addition, increasingly complex capital structures with multiple layers of secured debt can create opportunities for secured creditors to leverage their debt. Secured creditors can seek to influence the restructuring process and potentially seek to acquire certain assets of the debtor or the debtor as a going concern through a debt-for-equity exchange or a credit bid for some or all of the debtor's assets.
- **Landlords**. Beyond any rights granted under an applicable lease, landlords possess a common law right of distraint, allowing them to seize and sell assets located on a leased premise belonging to a tenant to recover rent arrears. However, the stay of proceedings under the CCAA and BIA (see *Question 6*) prevents landlords from exercising this remedy.

 

- **Government entities and regulatory bodies**. Under the CCAA and the proposal provisions of the BIA, a regulatory body is exempt from the scope of the stay of proceedings as it relates to investigations, actions, and other proceedings. However, on application by the debtor and with proper notice to the regulator and any affected parties, a court may order that the stay applies to all actions or steps taken by the regulator if a viable compromise or arrangement could not be made without that order and an order is not contrary to the public interest.
- **Employees**. While employee claims are typically unsecured pre-filing claims and are often compromised in restructuring proceedings, certain employee claims are granted limited priority and cannot be compromised under a proposal or plan. For example, a court cannot sanction a BIA proposal or CCAA plan that seeks to compromise these priority claims, and absent payment of all wages, salaries, commissions, or compensation for services provided after the commencement of the applicable proceedings.

### Influence on Outcome of Procedure

While the above stakeholders can influence the outcome of a restructuring or insolvency procedure, particularly the procedure a debtor company chooses, stakeholders' rights and interests are balanced within the broader framework of Canadian insolvency policy. Canadian courts have consistently interpreted the primary policy objective of Canadian insolvency legislation as facilitating restructurings where possible to avoid the significant social and economic consequences of bankruptcy or liquidation. Consistent with this objective, courts typically favour restructuring outcomes that preserve a business as a going concern if they present a reasonable prospect of preserving jobs and maintaining business operations.

## Liability

9. Can a director, partner, parent entity (domestic or foreign), or other party be held liable for an insolvent debtor's debts?

### Directors

Directors of a corporation will generally not be held liable for an insolvent corporation's debts. There are certain exceptions to this where, for policy reasons, certain Canadian statutes impose personal liability on corporate directors, including:

- Employee termination and severance pay, unpaid wages, or vacation pay.
- Environmental contamination.
- The corporation's obligations to collect, withhold, or remit Canada Pension Plan contributions, income tax, employment insurance, and sales and value-added taxes.

These statutory liabilities are not triggered by insolvency but often become a greater concern in times of financial distress as the company may be unable to pay its obligations.

 

### Partners

The liability of a partner for an insolvent partnership's liabilities depends on the type of partnership the partner is a part of:

- **General partnership.** Partners are jointly liable for all debts, liabilities, and obligations of the partnership.
- **Limited partnership.**A limited partnership consists of at least one general partner and one limited partner. The general partner is responsible for managing the limited partnership's business and has unlimited liability for all debts, liabilities, and obligations of the limited partnership. In contrast, the liability of a limited partner, who invests capital into the limited partnership but does not have an active role in the operations of the limited partnership's business, is limited to the amount of their capital investment in the partnership.
- **Limited liability partnership (LLP).** A partner in an LLP is generally not liable for the debts, obligations, and liabilities of the LLP. However, they are generally personally liable for liabilities arising from their own negligent or wrongful acts or omissions, or those of individuals under their direct supervision.

### Parent Entities (Domestic or Foreign)

A parent entity is typically (subject to certain exceptions) not liable for an insolvent subsidiary's debts or liabilities. It is common for a parent entity to enter into a contractual commitment and guarantee the obligations of a subsidiary.

### Other Parties

Certain third parties may become liable for the debts of an insolvent debtor. For example, where a guarantor becomes liable on the default of the insolvent debtor, subject to the terms of the guarantee.

Shareholders of an insolvent corporation will rarely be held personally liable for the debts and obligations of the insolvent corporation. In exceptional circumstances, Canadian courts will hold shareholders personally liable through a process known as "lifting" or "piercing the corporate veil."

## Setting Aside Transactions

10. Can an insolvent debtor's pre-insolvency transactions be set aside? If so, who can challenge these transactions, when and in what circumstances? Are third parties' rights affected?

Certain transactions may be challenged and set aside under the BIA by the trustee or under the CCAA by the court-appointed monitor, but these challenges to "pre-filing" transactions are relatively uncommon.

Two forms of reviewable transactions are preferences and transfers at undervalue, which are discussed below.

In addition, the payment of cash dividends, the redemption, or purchase for cancellation of shares, and certain forms of employment compensation to directors and officers may also be subject to a challenge if made within the year before bankruptcy or the commencement of restructuring proceedings where the debtor was insolvent at the time or was made insolvent by the payment.

Provincial legislation, such as Ontario's *Assignments and Preferences Act*, R.S.O. 1990, c. A.33 and *Fraudulent Conveyances Act*, R.S.O. 1990, c. F.29, also allows for the challenge of pre-bankruptcy transactions, regardless of whether a bankruptcy has occurred.

If a reviewable transaction is successfully challenged, directors and officers may be held personally liable.

### Preferences

Preferences are pre-filing transactions involving an insolvent debtor and a creditor, which result in a creditor receiving more than their proportionate share of the debtor's assets relative to what they would have received in a bankruptcy distribution. Preferences can take place in multiple forms, including payments, transfers of property, provision of services, or granting of a charge on a property to or in favour of one or more creditors at the expense of other creditors.

Courts may declare any such transaction in favour of an arms'-length creditor to be void if the transaction is made less than three months before the debtor's bankruptcy or commencement of restructuring proceedings with the intent to give that creditor a preference over other creditors. If the transaction has the effect of being preferential, there is a rebuttable presumption that it was made with the intent to prefer.

If the transaction is in favour of a non-arms'-length creditor, there is no requirement to prove an intention to prefer, and the applicable look-back period is extended to one year before the debtor's bankruptcy or commencement of restructuring proceedings.

### Transfers at Undervalue

A transfer at undervalue occurs when a debtor disposes of property or provides services for which no consideration is received by the debtor or for which the consideration received by the debtor is conspicuously less than fair market value. Courts may set aside these transactions or order that the recipient pay the difference between the value given and the value received if the following conditions are met:

- The debtor was insolvent at the time of the transaction.
- The transaction occurred in the year prior to the debtor's bankruptcy or commencement of restructuring proceedings.
- The debtor had intent to defraud or delay a creditor.

While proving the intent of the debtor to defeat creditors is difficult, courts may infer intent where the trustee or monitor establish the presence of "badges of fraud" associated with the transaction.

For transactions involving non-arms'-length parties, the relevant look-back period extends to five years. In these cases, there is also no requirement for the debtor to have intended to defraud or delay creditors or that the debtor was insolvent at the time of the transaction, if it occurred within one year of the bankruptcy or commencement of restructuring proceedings.

## Carrying on Business During Insolvency

11. In what circumstances can a debtor continue to carry on business during rescue or insolvency proceedings? In particular, who has the authority to supervise or carry on the debtor's business during the process and what restrictions apply?

Subject to any contrary court order, in a CCAA, BIA, or CBCA restructuring, the debtor company generally retains control and possession of its assets and continues to operate its business.

In a bankruptcy proceeding, on the issuance of a bankruptcy order or the filing of an assignment of bankruptcy, all of the assets of the bankrupt vest in a trustee in bankruptcy. At this point, the bankrupt no longer has any ability to deal with its assets or carry on its business. The trustee in bankruptcy rarely operates the business of the debtor but may require possession of the bankrupt's premises for some time while realising its property.

## Additional Finance

12. Can a debtor that is subject to insolvency proceedings obtain additional finance both as a legal and as a practical matter (for example, debtor-in-possession financing or equivalent)? Is special priority given to the repayment of this finance?

Debtors undergoing restructuring under the CCAA or BIA commonly seek court approval for DIP financing to finance their business and restructuring efforts. Both the CCAA and BIA empower courts to grant super priority charges over the debtor's property in respect of DIP financing. These charges can rank ahead of pre-filing secured creditors, provided notice was provided to the secured creditors.

The amount of DIP financing that a court can approve on an initial CCAA application is limited to what is reasonably necessary for the continued operation of the debtor in the ordinary course of business during the initial ten-day stay period. However, the amount of approved DIP financing is typically increased at the subsequent comeback hearing.

If interim financing is required in a CBCA proceeding, the parties typically address this contractually in advance as part of a restructuring support agreement. The CBCA does not specifically provide for the granting of priority charges.

## Multinational Cases where there are no Applicable EU or International Frameworks

13.What are the rules that govern a local court's recognition of concurrent foreign restructuring or insolvency procedures for a local debtor? Are there any international treaties or EU legislation governing this situation? What is the process for applying for local recognition where there are no applicable EU or international frameworks? What are the procedures for foreign creditors to submit claims in a local restructuring or insolvency process?

## Concurrent Proceedings and Recognition

The CCAA and BIA have established frameworks for recognising foreign insolvency and restructuring proceedings. Recognition proceedings in Canada are commenced by a foreign representative of the foreign proceedings, typically the debtor company or the entity responsible for supervising the foreign insolvency. The representative must demonstrate to the Canadian court that it is a "foreign representative," and that the application relates to a "foreign proceeding." Each of these terms are defined in the CCAA (section 45(1), CCAA) and BIA (section 268(1), BIA). If the Canadian court is satisfied, the court will classify the foreign proceedings as "foreign main proceedings" or "foreign non-main proceedings." This classification determines the scope of the relief available, with foreign main proceedings receiving greater protections.

Foreign main proceedings are proceedings that take place in the jurisdiction where the debtor has the centre of its main interests (COMI). The COMI is presumed to be the location of the debtor's registered office unless evidence to the contrary is provided. This determination must be made on an entity-by-entity basis. However, courts will consider the degree of integration between the entity and its corporate group when assessing the COMI.

Where a court is satisfied that the foreign proceedings are foreign main proceedings, the court must issue an order, under terms it deems appropriate, to grant the debtor company a stay of proceedings and prohibit the debtor company from selling or otherwise disposing of its property in Canada, except in the ordinary course of business. If the foreign proceedings are classified as foreign non-main proceedings, the court is not required to issue such an order but retains the discretion to do so.

In either foreign main proceedings or foreign non-main proceedings, the BIA and CCAA both provide the court broad discretion to make any order it considers appropriate, as long as the court is satisfied that the order is necessary to protect the debtor company's property, in the interest of a creditor or creditors, and not contrary to public policy.

## International Treaties

Canada has adopted the *UNCITRAL Model Law on Cross Border Insolvency*, which seeks to facilitate cross border insolvencies. In 2009, Canada amended both the BIA and CCAA to largely adopt the UNCITRAL Model Law on Cross Border Insolvency.

## Procedures for Foreign Creditors

Foreign creditors are not subject to any special or additional procedures when participating in Canadian insolvency or restructuring proceedings. They can file their claims using the same process available to Canadian creditors.

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