

Corporate Restructuring Law Primer: Solutions to Assist Businesses Impacted by COVID-19



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A. Introduction

On March 17, 2020, the provincial government declared a state of emergency in British Columbia due to the novel coronavirus (COVID-19). Various measures were instituted both federally and provincially to reduce the harmful economic effects of COVID-19. Nonetheless, the unfortunate reality is that many businesses still face tough decisions regarding their ability to continue, or recommence, operations at present and the ability to rebound as COVID-19 restrictions are lessened and post-COVID-19 activity resumes. As a result, businesses will be compelled to consider insolvency options. The term “insolvency” is frequently associated with the collapse of a business and bankruptcy; however, insolvency laws also provide the framework to restructure, reorganize and avoid bankruptcy proceedings, which businesses can utilize to survive the consequences of COVID-19.

Specifically, a Division 1 Proposal under the *Bankruptcy and Insolvency Act* (“BIA”) and the *Companies’ Creditors Arrangement Act* (“CCAA”) are the

primary federal laws designed to give companies an opportunity to restructure their business and financial affairs and negotiate payment arrangements with their creditors.

B. BIA Division 1 Proposal

The term “bankruptcy” in the *BIA* may lead to the assumption that the *BIA* is only available if a company is bankrupt or intends to file for bankruptcy. This is incorrect. The *BIA* also provides a restructuring regime (known as a Division 1 Proposal).

- Who is eligible?

A Division 1 Proposal may be filed by an insolvent company or an individual (we will focus on the Division 1 Proposal filed by a company). There is no aggregate threshold with respect to the amount of creditor claims a company must have against it before it may file a Division 1 Proposal.

- How is a Division 1 Proposal initiated?

A Division 1 Proposal is initiated by filing a Notice of Intention to File a Proposal (the “NOI”) at the Office of the Superintendent of Bankruptcy. A company will need to retain the assistance of a licensed insolvency trustee (the “Trustee”) to file the NOI.

Upon filing the NOI there is a stay of proceedings with respect to claims by creditors¹ against the company and claims against its’ directors². A stay of proceedings suspends ongoing and future legal proceedings. The stay applies to both unsecured creditors and secured creditors (if the secured creditors have not met the notice requirements under section 244 of the *BIA*).³ A stay of proceedings is effective until the filing of the proposal.

- What happens after the NOI is filed?

Within 21 days of the filing the NOI, the Trustee will hold a meeting of the company’s creditors.⁵ At the meeting the Trustee will present the company’s proposal to the creditors which is essentially an agreement between the company and its creditors to compromise their legal claims. There are no requirements with respect to the type of agreement that may be offered. Common types of agreements that may be offered by a company to its creditors are: (1) payment of X amount to be shared *pro rata* within each class of creditors; (2) partial payment of X “cents on the dollar”; (3) a liquidation plan where the company’s assets are sold; or (4) delivery of shares in the company in exchange for debt or a combination of cash and shares.



“...the unfortunate reality is that many businesses still face tough decisions regarding their ability to continue, or recommence operations at present...”

The proposal must be approved by the majority of creditors in each class and the majority of creditors in each class must hold at least 2/3 of the total dollar value of debt in the class.⁶ If creditors approve the proposal then it will be subject to approval by the court.⁷ Upon successful completion of the proposal the company is legally released from the claims included in the proposal.

- What happens if the creditors do not approve the Proposal?

If the proposal is not approved, the company is automatically assigned into bankruptcy.⁸

C. CCAA Proceeding

- Who is eligible?

A CCAA proceeding can be initiated by an insolvent Canadian company, or foreign company with assets or doing business in Canada, that has creditor claims against it (or its affiliate(s)) of over \$5 million.⁹

- How is a CCAA proceeding initiated?

A CCAA proceeding is initiated by an application to the court for a court order granting the company protection pursuant to the

CCAA (known as the “Initial Order”). If the court is satisfied that a CCAA proceeding is appropriate, it will make the Initial Order.

Among other terms, the Initial Order will appoint a Monitor and order a stay of proceedings against the company.¹⁰ The stay is initially effective for 10 days.¹¹ However, it may be extended further by

¹ *Bankruptcy and Insolvency Act*, R.S.C., 1985, c. B-3 [BIA], s. 69

² *BIA*, s. 69.31

³ *BIA*, ss. 69(2) and 244

⁴ *BIA*, s. 69(1)

⁵ *BIA*, s. 51

⁶ *BIA*, s. 54

⁷ *BIA*, s. 58

⁸ *BIA*, s. 57

⁹ *Companies’ Creditors Arrangement Act*, R.S.C., 1985, c. C-36 [CCAA], ss. 1 and 3

¹⁰ *CCAA*, s. 11.02(1)

¹¹ *CCAA*, s. 11.02(1)

court application.¹² A Monitor is an independent party who acts as the court's "eyes and ears" and it provides reports to the court and the creditors regarding the company's progress in restructuring its affairs.

- What happens after the Initial Order?

The company will work with the Monitor to formulate a plan of arrangement (the "Plan"). The Plan is similar to a proposal made under a Division 1 Proposal. It provides the same flexibility to the company in proposing terms with its creditors (examples are set out above).

Similar to the voting requirements under a Division 1 Proposal, the Plan must be approved by the majority of creditors in each class and the majority of creditors in each class must hold at least 2/3 of the total dollar value of debt in the class.¹³ If it meets creditor approval, it will be subject to approval by the court.¹⁴ Upon successful completion of the Plan the company is legally released from the claims included in the Plan.

- What happens if the creditors do not approve the Plan?

Unlike a Division 1 Proposal, the company does not automatically become bankrupt if the Plan is not approved by its creditors. However, the stay of proceedings will be lifted and creditors may pursue an action against the company for their respective debts. This will likely place the company into the same position it was in when it originally sought CCAA protection and may compel it to file for bankruptcy.

D. Potential Advantages of Filing a Division 1 Proposal or CCAA Proceeding

A company may utilize the following mechanisms to its advantage under a Division 1 Proposal or a CCAA proceeding:

- Continued management of business: the company remains in charge of its assets and continues to manage its day to day operations (with oversight by the Trustee or the Monitor).

¹² CCAA, s. 11.02(2)

¹³ CCAA, s. 6(1)

¹⁴ CCAA, s. 6(1)

¹⁵ CCAA, s. 11.2(1)

¹⁶ BIA, s. 50.6

¹⁷ BIA, s. 65.11(1)

¹⁸ CCAA, s. 32

¹⁹ BIA, s. 65.2



- Stay of proceedings: the company continues its day to day operations without the disruption and upheaval caused by legal actions against it.
- Compromised payment agreement: the company and its creditors can both benefit from entering into a compromised repayment plan. Payment terms are tailored to the company's actual ability to pay and creditors will likely receive greater payment in comparison to payment under bankruptcy proceedings.
- Interim financing: under the CCAA, the court may order that the company receive additional financing (known as debtor-in-possession financing) so that the lender obtains a "super priority" status;¹⁵ i.e. the lender will have the first claim to the assets of the company if the restructuring process is ultimately unsuccessful. Under a Division 1 Proposal, the court may also order that additional financing be secured by the company's property in priority to other creditors.¹⁶ This allows a company to access funds a lender may otherwise withhold.
- Disclaimer of contracts: the company may disclaim (i.e. terminate) a contract to which it was a party at the time it filed the NOI¹⁷ or CCAA proceeding, subject to challenges by the other party.¹⁸ This allows a company to terminate unprofitable contracts.
- Disclaimer of lease: under a Division 1 Proposal, the company may disclaim (i.e. terminate) a commercial lease upon 30 days notice, subject to a challenge by the landlord.¹⁹

- Declaration of critical supplier: under the CCAA, the court may deem a supplier a “critical supplier” and require it to keep supplying goods and services to the company on terms and conditions that are consistent with the supply relationship or that the court considers appropriate.²⁰

E. BIA Assignment into Bankruptcy

If a Division 1 Proposal under the BIA or a Plan under the CCAA is not a workable solution for a company, it may assign itself into bankruptcy which effectively signals the end of the business. In general terms, the Trustee will collect the company’s assets, sell the assets and distribute the sale proceeds from said assets to creditors in accordance with the applicable BIA provisions.

²⁰ CCAA, s. 11.4

F. Conclusion

In light of the economic effects of COVID-19, and the uncertainty of its duration and fallout, a proactive company will consider all available restructuring remedies. This includes potentially utilizing the BIA and CCAA to restructure and reorganize its operations. Both regimes offer the ability to successfully navigate the complications that will arise from COVID-19 and provide a company with a foundation to revive operations and begin a fresh start.

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