TRONDHEIM QUESTIONNAIRE

1. Are there any specific regulations respecting insolvency proceedings?

Bankruptcy and insolvency are federally regulated. The following federal statues apply to bankruptcy and insolvency proceedings:

The ***Bankruptcy and Insolvency Act*** (BIA) provides the legislative framework for the liquidation of assets. It applies to individuals, partnerships and corporations. Under the BIA, a trustee is appointed to take charge of the assets, sell them and distribute the proceeds.

The ***Companies' Creditors Arrangement Act*** (CCAA) governs the reorganization of insolvent companies. Under the CCAA, a court may stay any action by creditors against the insolvent corporation while it negotiates with them for the rescheduling or compromise of its debts. Pursuant to s. 3(1), the CCAA only applies where the debtor company satisfies the threshold requirement of debt exceeding $5 million.

The ***Winding-up and Restructuring Act*** governs the liquidation of financial institutions (e.g. banks, insurance companies, trust and loan companies), which cannot be liquidated under the BIA.

The ***Wage Earner Protection Program Act*** (**Not yet in force**) establishes the Wage Earner Protection Program (WEPP) to pay wages owed to employees by employers who are bankrupt or subject to receivership.

2. Which institutions (government agencies, courts, etc.) are in charge of insolvency proceedings generally and which institutions are in charge of the resolution of conflicts related to employment law.

With respect to bankruptcies, the Superintendent of Bankruptcy is charged with ensuring that bankruptcies and insolvencies in Canada are conducted in a fair and orderly manner. The Superintendent is responsible for licensing and supervising bankruptcy trustees.

With respect to the resolution of conflicts that arise in the context of employment, the relevant institution is the respective provincial labour relations board (LRB).

Courts of law are also involved in the process. For example, courts are responsible for issuing certain orders under the BIA, or approving various actions by companies or creditors. The CCAA grants the courts considerable judicial flexibility in proceedings involving insolvent corporations. Further, courts may also become involved in disputes arising from decisions made by the Superintendent or the LRB.

3. Are employment contracts automatically terminated upon bankruptcy or insolvency of the employer, or do they remain in force?

Upon the bankruptcy of an employer, the employment contract is deemed to have been terminated by the act of the employer, thus entitling employees to notice or wages in lieu thereof.[1]

However, the employment contracts may persist for a period of time. While not obliged, a trustee in bankruptcy may, when necessary, carry on business of the bankrupt until the first meeting of creditors (BIA, ss.18 and 22). Indeed, it is not uncommon for trustees to hire employees on a per diem basis to perform work necessary for liquidation of the company's assets.

Further, in the event that the trustee sells the bankrupt company as a going concern, the purchaser may rehire some or all or some of the employees.[2] In the absence of a collective agreement, the purchaser is entitled to renegotiate the employment contract. Where there is a collective agreement, the purchaser is deemed a successor employer and is thus bound by the terms of the collective agreement when dealing with the employees of the bankrupt.[3]

The situation with respect to employment contracts of an insolvent company or one for which a receiver is appointed by the court is somewhat different. Where a company enters insolvency, it may continue to operate and employ its workers. The insolvency administrator will typically borrow money or seek the approval of secured creditors with security over the debtor's assets to allow wages to be paid and ensure continuity of the business.[4] The fate of workers in the restructuring will be decided by the proposal the insolvent company puts to its creditors (i.e. whether and to what extent the company will downsize through layoffs, etc.).

In a unionized context, where a receiver is appointed, the receiver is deemed to step into the shoes of the bankrupt employer and thus becomes a successor employer bound by the terms of the collective agreement.[5]

4. Where an employment contract is automatically terminated, are the employees entitled to any severance or other benefits?

As noted above, non-unionized employees are deemed terminated by the employer without cause upon bankruptcy and thus are entitled to notice or wages in lieu thereof. Employees are entitled to unpaid wages in accordance with s.136 of the BIA (see question 6). However, with respect to additional claims, such as claims for payment in lieu of notice, employees are considered unsecured creditors who recover on a pro rata basis with other unsecured creditors.[6]

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[1] *Rizzo v. Rizzo Shoes Ltd*., [1998] S.C.J. No. 2; *Stanton v. Reliable Printing Ltd*. (1998), 61 Alta L.R. (3d) 398, 1998 ABQB 83.
[2] *Radwan v. Arteif Furniture Manufacturing Inc*., [2002] A.J. No. 1031, 2002 ABQB 742.
[3] *Saan Stores Ltd. V. United Steelworkers of America, Local 596 (Retail Wholesale Canada, Canadian Services Division)* (1999), 172 D.L.R. (4th) 134 (NSCA).
[4] E. Patrick Shea, *Bill C-55 Commentary* (Markham: Butterworths, 2006).
[5] *GMAC Commercial Credit Corporation – Canada v. T.C.T. Logistics Inc*., [2006] 2 S.C.R. 136, 2006 SCC 35.
[6] See *Rizzo* and *Stanton*.

5. Can the employment contract be terminated once bankruptcy or insolvency proceedings have occurred? Upon what basis? Is the employee entitled to severance or any other benefit?

If the business continues to operate, either under the direction of a trustee, insolvency administrator or receiver, non-unionized employees could be terminated at any time, subject to the appropriate notice requirements. Termination of unionized employees would have to be done in accordance with the collective agreement.

The amendments in Bill C-55 would strengthen these protections for unionized employees. Specifically, the proposed provisions make clear that collective agreements cannot be assigned or disclaimed by a bankrupt employer without the union's consent, but rather will remain in force after initiation of insolvency proceedings. Further, the collective agreement cannot be amended except in accordance with the terms of the BIA or CACA, or with the laws of the governing jurisdiction. The employer cannot unilaterally affect the collective agreement. As a result, the employer's only option is to seek the court's permission to serve notice to bargain.

6. What privileges or preferences, if any, are granted to employment credits?

Relevant Provisions under the BIA:

Under the BIA priorities scheme, employees (or wage earners) are ranked ahead of ordinary creditors but behind secured creditors. Section 136(1)(d) of the BIA gives preferred status to up to $2,000 in wage claims for services provided in the six months immediately preceding the employer's bankruptcy. Additionally, this section allows priority for up to $1,000 for disbursements for salespeople. It should be noted that claims made under this section are considered unsecured claims and therefore subject to the rights of secured creditors.

Section 60(1.3) of the BIA further provides that a proposal by an insolvent company under the BIA will not be approved unless it provides for payments to the employees and former employees of amounts equal to the amounts that they would be qualified to receive under s. 136 if the employer became bankrupt.

The BIA is relatively silent on other employment issues, which are determined by the applicable federal or provincial legislation pursuant to s.72(1) of the BIA, or under the inherent jurisdiction of bankruptcy courts.[7]

[7] Section 72(1) reads as follows:

72. (1) The provisions of this Act shall not be deemed to abrogate or supersede the substantive provisions of any other law or statute relating to property and civil rights that are not in conflict with this Act, and the trustee is entitled to avail himself of all rights and remedies provided by that law or statute as supplementary to and in addition to the rights and remedies provided by this Act.

Case Law:

The recent decision of the Supreme Court of Canada in *TCT Logistics* has important implications for the treatment of employee claims and illustrates how priority as set out in the BIA can be disturbed.[8] Specifically, if a receiver manager is appointed to administer an insolvent company, employee wages and benefits may take priority over even secured creditors.

In this case, the Supreme Court of Canada allowed an application for successorship to be brought against a receiver. The facts were that KPMG was appointed interim receiver of TCT Logistics under an order that authorized KPMG to dispose of all or part of TCT's assets. The order further declared that KPMG was not a successor employer of TCT and therefore was not bound by the collective agreement between TCT and the union. Upon appointment, KPMG terminated the existing employment contracts, and rehired some employees on substantially different terms. The union subsequently sought leave to bring an action against KPMG, GMAC and others for breach of the collective agreement. The SCC's decision to allow the union to bring the application is important in two respects. First, it makes clear that the BIA does not confer power on bankruptcy courts to alter or modify pre-bankruptcy union or employment rights as these continue to be governed by provincial law. Second, the SCC made clear that trustees and secured creditors cannot dispose of the debtor's enterprise without the buyer being treated as a successor employer.

The government has attempted to achieve some consistency with Bill C-55. Bill C-55[9] was given Royal Assent in 2005 but has not yet come into force. Bill C-55 would have a significant impact on employee rights because it:

- defines priorities for employee and pension claims in liquidating bankruptcies and receiverships;
- stipulates minimum payments to employees and in respect of pension plans in the context of a plan of compromise or arrangement under ss. 6(4) or (5) of the CCAA (brings CCAA in line with BIA); and
- ranks employee wages for services rendered in the 6 months immediately preceding the bankruptcy, or the 1st day of the appointment of a receiver, to a maximum of $2000, in priority to secured creditors;

Miscellaneous Provisions:

Section 427 of the federal *Bank Act* gives claims for wages earned within three months before bankruptcy a priority over a security interest which a bank may have taken under that section. However, this provision is easily avoided by taking a security interest under provincial legislation.

Although provincial legislation may allow statutory security interests and deemed trusts covering wage claims, thereby giving them priority over the claims of secured creditors, the devices often do not operate in bankruptcy because the BIA provisions take precedence over provincial wage legislation and limit wage claims to a preferred status.

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[8] *GMAC Commercial Credit Corporation – Canada v. T.C.T. Logistics Inc.*, [2006] 2 S.C.R. 136, 2006 SCC 35.

[9] S.C. 2005, c.47

Wage earners may also be protected under s.119 of the *Canada Business Corporations Act*, which imposes liability on a company's directors for up to six month's unpaid wages for services performed (but not termination pay). Further, under s.251.18 of the Canada Labour Code, directors are jointly and severally liable for wages and termination/severance pay to a maximum of the equivalent of six month's wages.

Pension fund claims are better protected in bankruptcies than wage claims because relatively strong priorities have been accorded to such claims. Upon bankruptcy, an employer may face claims for unremitted employer pension fund contributions, employee contributions deducted by the employer but not remitted to the fund, and unfunded liabilities arising when returns on investment are insufficient for the fund to meet its obligations. While the BIA does not assign express priority to pension fund claims, they are protected under federal and provincial pension legislation.

For example, s.8(2) of the federal *Pension Benefits Standards Act* (PBSA) deems employer and employee pension contributions to be held in trust if the employer becomes bankrupt. Provincial legislation has a similar effect and gives the pension fund a lien against the employer's assets in the event of bankruptcy.

7. Is there a guarantee institution that takes charge of the debts unpaid by the insolvent employer and to what extent?

While there is currently no guarantee institution that employees can rely on, there may be in the future if the *Wage Earner Protection Program Act* is brought into force. The proposed Wage Earner Protection Program (WEPP), established under the Act, guarantees payment of workers' wages in the event that the employer becomes bankrupt or subject to a receivership (s.4). Wages are paid out of a Consolidated Revenue Fund (s. 35). Specifically, WEPP would pay employees' wages earned during the six months prior to the date of bankruptcy or the appointment of a receiver, to a maximum of the greater of $3,000 or an amount equal to four times the maximum weekly insurable earnings under the *Employment Insurance Act*.

"Wages" are defined in the act to include salaries, commissions, compensation for services rendered, vacation pay and any other amounts prescribed by regulation but do not include severance or termination pay. Payment is no long dependent upon the employers' assets and would be provided quickly to employee claimants. The federal government estimates that up to 97% of unpaid wage claims would be fully paid under the WEPP.

8. Is the guarantee institution subrogated in the rights and/or privileges granted to the worker, and may claim for them during the insolvency proceedings?

Section 36(1) of the *Wage Earner Protection Program Act* grants the government subrogation rights in respect of all claims paid in respect of unpaid wages:

36. (1) If a payment is made under this Act to an individual in respect of unpaid wages, Her Majesty in right of Canada is, to the extent of the amount of the payment,

subrogated to any rights the individual may have in respect of those unpaid wages against

(*a*) the bankrupt or insolvent employer; and

(*b*) if the bankrupt or insolvent employer is a corporation, a director of the corporation.

(2) For the purposes of subsection (1), Her Majesty in right of Canada may maintain an action against a bankrupt or insolvent employer, or a director, either in the name of the individual referred to in that subsection or in the name of Her Majesty in right of Canada.

9. What other effect, if any, does the insolvency proceeding on the employment relationship?

n/a

10. When the whole or part of the enterprise is transferred during an insolvency proceeding, what affect does this have on employees' rights?

As noted above, if the trustee in bankruptcy sells the business of the bankrupt employer as a going concern, the purchaser may rehire some or all of the employees. The test for "going concern" is whether there was continuity of business, as illustrated by several factors. The benefit to an employee of a finding that the business was sold as a going concern is that if, the employee is rehired by the purchaser and subsequently terminated, s/he is entitled to credit for his/her previous employment with the bankrupt employer when determining the appropriate notice period.[10]

As noted above, where the employees of the bankrupt or insolvent business are unionized, a transfer will be deemed a disposition giving rise to successorship rights, pursuant to the relevant labour relations legislation. The Supreme Court made clear in *TCT Logistics* that trustees and secured creditors cannot dispose of the debtor's enterprise without the buyer being treated as a successor employer.

11. Are there specific regulations protecting employees if an enterprise is shut down or if there are mass dismissals? Describe them.

There do not appear to be any specific regulations protecting employees if a business is shut down or there are mass dismissals due to bankruptcy or insolvency. Employees are entitled to unpaid wages as guaranteed under s.136 of the BIA. In respect of all other claims, employees are deemed to be unsecured creditors and entitled to be paid on a pro rata basis with the other unsecured creditors.

While some the federal government and some provinces provide special notice periods and impose other obligations on employers who dismiss a large number of employees at the same time, Alberta has not followed suit. The Employment Standards Code in Alberta merely requires that the employer give the Minister 4

[10] *Radwan v. Arteif Furniture Manufacturing Inc*., [2002] A.J. No. 1031, 2002 ABQB 742.

weeks' written notice if it intends to terminate the employment of 50 or more employees at a single location. The written notice must specify the number of employees who will be terminated and the effective date of the terminations. The only exception is in relation to seasonal workers or employees hired for a specific term or task. It does not appear that s.137 affords employees any greater benefit in terms of notice or termination pay in the event of a mass dismissal.