By PAUL MACDONALD & BRETT HARRISON

Where do we go from here?

COURTS WILL BE REVIEWING RECEIVERSHIP ORDERS MORE CLOSELY AND INSOLVENCY PRACTITIONERS SHOULD BE READY TO JUSTIFY THE RELIEF SOUGHT

CATHY PENTLAND

Since the early 1990s — when the provisions of the Bankruptcy and Insolvency Act (BIA) were expanded to provide receivers with increased powers and a Commercial List was established in Toronto to hear receivership matters — the use of court appointed receivers has increased dramatically. 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 sophisticated 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 that had previously been regularly granted. As a result, insolvency practitioners will have to take a hard look at the powers the courts will grant to a receiver and re-evaluate their use.

An attempt has been made to address some of these issues, and to standardize the form of receivership orders, by the Commercial List users' committee's subcommittee for Standard Form Template Orders, which recently finalized a model receivership order.

First move to restrict receivership orders

The mix of broad, potentially unnecessary powers and the ex parte nature of the orders granting them have made some courts question both the need for such orders and the courts' authority to grant them. In the insolvency of Big Sky Living Inc., Justice F. Slatter of the Alberta Court of

Queen's Bench took issue with an ex parte interim receivership order and questioned what was truly necessary for the protection of the estate or the creditors.

Judge Slatter objected to the breadth of the order and its forward-looking approach. He 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, the judge held that the following provisions in the draft order were inappropriate and should not be granted on an ex parte basis:

- exempting the interim receiver from compliance with the notice requirements of the (Alberta) Personal Property Security Act;
- authorizing the interim receiver to assign the debtor into bankruptcy and to act as trustee in bankruptcy;
- restraining contracting parties from terminating, ceasing to perform or altering contracts with the debtor;
- declaring employees to be terminated and stipulating that the interim receiver would not be a successor employer; and
- limiting the liability of the interim receiver to the net realizable value of the debtor's assets.

Big Sky comes to Ontario

Although Ontario courts continue to grant very broad receivership orders, there are signs the tide may be turning. In *GMAC Commercial Credit Corp. of Canada v. T.C.T. Logistics Inc.*, the appeal court addressed the issue of whether the bankruptcy court had the authority under the BIA to relieve the receiver from successor employer obligations imposed under applicable labour legislation.

Judge Kathryn Feldman, speaking for two of the three members of the appeal panel, found that the broad language in Section 47(2) did not provide support for trumping rights created under provincial statutes. Counsel for the receiver argued that failing to grant interim receivers this protection would force them to wind up a business even if this would not provide an optimal outcome for stakeholders, as interim receivers (and the secured creditors who typically backstop them) would not want to be exposed to personal liability for costly employee obligations. In response to this the judge stated:

"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."

Most importantly, Judge Feldman affirmed the judgment in Big Sky and 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.

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

Model order

In 2003 the subcommittee, comprised of insolvency lawyers, commenced the task of developing the Model Order.

Although the Model Order is meant to be a starting point, not a rigid template from which one can't deviate, the subcommittee asked that if counsel adopted provisions that depart from the Model Order, they should bring these changes to the attention of the court. Since the Commercial List appears to be rapidly adopting the Model Order, it would be wise to ensure that you can explain to the court the reasons for any variations sought by the interim receiver to the Model Order.

Preliminary matters

The Model Order provides for the appointment of both an interim receiver under Section 47(1) or 47.1 of the BIA and a receiver and manager under Section 101 of the Courts of Justice Act (CJA). The reasons include:

- an order appointing an interim receiver under the BIA has national scope;
- a receiver and manager under the CJA can be provided with a priming charge in respect of its disbursements; and
- a CJA receivership order is not stayed if it is appealed, a BIA order is stayed.

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 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 subcommittee felt that bankruptcy was a sufficiently material, substantive and final act that the approval of the court should be obtained at the appropriate time.

Injunctions, possession, access to property

The Model Order requires every person 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 property as the receiver requires. Limiting the obligation to deliver up the debtor's property to only those cases where the receiver requires the property should save costs for the third parties and protect the estate from being forced to incur costs to move or store unnecessary property.

Stay of proceedings

The Model Order provides specific stay-related relief, but attempts to clean up some 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

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- 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 counterparties to renew contracts with the debtor. Instead, third parties are restricted only from failing to "honour renewal rights."

In a compromise with government representatives, the subcommittee agreed to build in an exception so that the receiver is not exempt from complying with statutory and regulatory provisions relating to health, safety or the environment.

Environmental issues

Although the Model Order does not immunize the receiver against a finding that it has occupied, possessed or taken control of a property, it does provide that the receiver is not required by the order to "occupy or take control, have, charge, possession or management of any property that might be environmentally contaminated." Accordingly, the receiver can only incur liability for environmental harm that occurs after its appointment when the receiver chooses to take possession of environmentally contaminated property.

Employment issues

In light of the fact that the Ontario Court of Appeal has held that successor employer protection is not authorized by Section 47, the Model Order does not provide this protection to the interim receiver. It adopts a minimalist approach by authorizing the hiring of employees and reiterating the protections in subsection 14.06(1.2), but otherwise awaits new developments in this area of the law.

PIPEDA

The Model Order contains a provision that entitles the receiver to disclose personal information to prospective purchasers under the terms of appropriate confidentiality orders. But if the prospective purchaser does not complete the sale, he or she must maintain confidentiality and destroy or return to the receiver all information.

Receiver's liability

The Model Order protects the receiver from litigation by a stay provision and ensures that the receiver will only be liable for clear acts of misconduct. Gross negligence/willful misconduct has been continued as the standard of culpability in order to limit the ability of creditors to mount a challenge to the reasonableness of every exercise of the receiver's discretion.

Funding of the receivership

The Model Order provides for two priming charges — a charge for the receiver's fees and those of its counsel and a charge in respect of any borrowings made by the receiver. Of course, the particular circumstances of each case will dictate the nature, number and priority of other charges that may be appropriate in any given case.

The future

The decisions in Re Big Sky Living and T.C.T. Logistics make it clear that courts will be reviewing receivership orders more closely in the future and insolvency practitioners should be ready to justify the relief sought, especially if it affects the rights of third parties who have not been served. It is now more likely that courts will ask receivers to rely on the protections of Section 215 of the BIA, rather than grant blanket immunity in the appointment order. The problem with this is that receivers may not know whether they are exposed to liability until it is too late.

The Model Order is not likely to spell the end for receivers but may cause a change in strategy. Where possible, parties will probably attempt to prepare prepackaged sales of the assets in order to limit the receiver's managerial role. It is also likely using the CCAA for restructurings and/or liquidations will become more prevalent as it provides a mechanism to restructure or liquidate a debtor's assets without going into possession.

Lastly, although the use of the Model Order will assist in the process of standardizing receivership orders, it will have to be a dynamic document that changes as the law develops, as we are likely at the beginning, not the end, of the courts' review of the scope of receivership orders.

Paul Macdonald is a partner and Brett Harrison is an associate with McMillan Binch LLP. They are in the commercial litigation and restructuring departments

Technical editor: Peter Farkas, CBV, CIRP, CA, vice-president, Richter & Partners Inc.