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OVERVIEW OF THE CURRENT STATUS OF UNSECURED CREDITORS' COMMITTEES IN CANADA

By

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I. INTRODUCTION

[1] Insolvency proceedings in Canada enable debtor companies to restructure or to liquidate either in debtor-in-possession proceedings under the *Companies' Creditors Arrangement Act*, RSC 1985, c. C-36 (the "CCAA") or in bankruptcy under the *Bankruptcy and Insolvency Act*, RSC 1985, c. B-3 (the "BIA"). Since most of the recent developments relating to representation of unsecured creditors in insolvency have arisen in the context of CCAA proceedings, this commentary focusses primarily on that legislation, and does not discuss, for example, the roles and duties of inspectors on behalf of creditors under the BIA.

[2] To set the context, and in gross summary, under the CCAA, the debtor company retains control of its business with the protection of a stay during a period of restructuring, under the control and oversight of the Court and with the assistance of a Court-appointed officer, the Monitor, who acts as the eyes and ears of the Court and serves as a liaison between the debtor and creditors. The period of restructuring ends with the creditors voting on a restructuring plan which, if approved by the creditors, must then be sanctioned by the Court.

[3] Again in summary, the scope of the Monitor's involvement in the restructuring process may vary. The CCAA is distinguishable from the more structured insolvency statutes of other jurisdictions by its relative brevity, and by the fact that it has been interpreted to give broad, discretionary powers to the Court.

[4] This commentary borrows heavily from two excellent articles recently published in the Annual Review of Insolvency Law 2011, Janis P. Sarra, Editor, 2012 Thomson Reuters Canada Limited:

(a) Ad Hoc Creditors' Committees in CCAA Proceedings: The Result of a Changing and Expanding Restructuring World - Robert J. Chadwick and Derek R. Bulas

(b) Enhancing the Role of Creditors' Committees in Corporate Rescue Laws - Jason Harris

II. CREDITORS' COMMITTEES IN CCAA PROCEEDINGS

[5] There are no statutory provisions under the CCAA or the BIA for the appointment of creditors' committees or representative counsel in an insolvency, whether on behalf of unsecured creditors or otherwise. However, it has become relatively common in the last ten years for the Courts in Canada to use their discretionary power to recognize and accept submissions from ad hoc committees that involve different classes of note or bond holders or in large receiverships or proceedings under the BIA where there are numerous investors in one or more commercial real estate projects.

[6] The earliest recognition of creditors' committees was primarily on an ad hoc basis in CCAA proceedings involving such large restructurings as Air Canada in 2003, Stelco in 2004 and Calpine in 2005, with the recognition and involvement of such committees in restructurings becoming more prevalent in 2008 to 2011. In the earlier years, these committees were usually self-funded.

[7] Effective in 2009, the CCAA and the BIA were amended to codify the developing practice of allowing security for the payment of professional fees and expenses of such committees. Section 11.52(1)(c) of the CCAA now permits the Court, on notice to secured creditors who are likely to be affected, to make an order declaring all or part of the property of the debtor company subject to a security or a change in an amount in the discretion of the Court for such professional fees if the Court is satisfied that such security is necessary for the effective participation of interested persons in proceedings under the Act.

[8] Charges pursuant to Section 11.52(1)(c) have been granted in favour of ad hoc unsecured note holder committees in the Canwest proceedings in 2009 and in Angiotech in 2011. While there are no statutory criteria the Court should take into account in deciding whether to order such a charge, the Courts have referred to factors such as the size and complexity of the business being restructured; the proposed role of the beneficiaries of the charge; whether there is an unwarranted duplication of roles; whether the quantum of the change appears to be fair and reasonable; the position of the secured creditors likely to be affected by the charge; and the recommendation of the Monitor on the issue: *Re Canwest Publishing Inc./Publications Canwest Inc.* (2010), 63 CBR (5^{th}) 115 (Ont.Sup.Ct.) at para. 54.

[9] Section 11.52(1)(c) has also been used to appoint and fund representative counsel for vulnerable creditors such as employees and retirees: *Re Nortel Networks Corp* (2009), 53 CBR (5^{th}) 196, also (2009, 55 BCR (5^{th}) 114 (Ont. Sup. Ct.); *Re Fraser Papers Inc.*, 2009 CarswellOnt 6169 (Ont.Sup.Ct.).

[10] Section 11.52(1)(c) has been invoked to fund professional support for unsecured creditor committees made up of representatives of disgruntled investors in large commercial real estate receiverships and CCAA proceedings, including the Concrete Equities Group in 2009 and more recently, the Legacy Group in January, 2012. In these cases, the unsecured creditors' committees have asked the Court to approve by-laws and appoint the initial members of the committee. The

by-laws vary in detail, but in these types of cases may include an indemnity for the members of the committee relating to costs and expenses, and provisions for the removal and replacement of members.

III. DIFFERENCES BETWEEN THE CANADIAN EXPERIENCE AND UNSECURED CREDITORS COMMITTEES UNDER U.S. BANKRUPTCY LAW

[11] The main reason why unsecured creditors' committees are not as prevalent in Canada as they are in the U.S. is because of the role of the Monitor in CCAA proceedings. As noted previously, the Monitor is an officer of the Court, with fiduciary responsibilities to both the debtor and creditors and a duty to act honestly and in good faith and in compliance with a statutorily-mandated Code of Ethics. The Monitor must report regularly to the Court, provide creditors with information and give an opinion with respect to the reasonableness and fairness of the plan that is eventually presented to the creditors for approval. The Monitor is the "good sheriff" who must look out for the reasonable interests of all stakeholders. Thus, in many cases, an unsecured creditors' committee may be unnecessary, and may only serve to make a restructuring more expensive. However, the Monitor is not a negotiator for any one group of creditors, and therefore it is becoming increasingly common to see ad hoc committees of unsecured creditors in situations where there are substantial assets and competing groups of bondholders or investors in particular projects. It is also more common to see these committees in cross-border restructurings where there are ad hoc and official unsecured creditors' committees appointed under Chapter 11 proceedings.

[12] Another key difference is that Canadian unsecured creditors' committees are not supervised or appointed by a governing body, as are official UCCs in the U.S. While the Court may approve their appointment in Canada, members are free to join or withdraw at will: Chadwick and Bulas at 127.

[13] It is generally accepted that members of Canadian ad hoc committees do not have fiduciary duties to similarly situated creditors, although this assumption has not yet been tested before the Courts. This is in contrast to the fiduciary duties imposed on members of U.S. official committees to members of the class of creditors that they represent, and possibly to others: Ibid at 128.

[14] While U.S. bankruptcy courts are accustomed to approving measures that are designed to provide a "chinese wall" between members of the official UCC and such members' security trading branches, members of Canadian ad hoc committees are not usually entitled to receive material non-public information without agreeing to terms of confidentiality and accepting the limitations on trading such access may entail: Ibid at 129.

IV. ISSUES AND CHALLENGES

[15] Since ad hoc creditors' committees in Canada are largely self-formed and unsupervised by the Court except on a high level, issues of governance can arise that have the potential of impeding, rather than aiding, efficient and responsive negotiation among stakeholders towards a viable plan.

[16] The CCA does not have an equivalent provision to U.S. Bankruptcy Rule 2019 which attempts to address disclosure of creditors' economic interests, and the Courts in Canada have not yet directly addressed the problems that may arise from turnover of committee members during the course of a restructuring as a result of trading of debt. This issue, however, has begun to attract attention. How these issues of accountability and transparency will be resolved in Canada is still uncertain.

[17] The perceived lack of fiduciary duty to similarly situated creditors has resulted in committees that are free to advance their own interests. As Chadwick and Bulas put it at page 133:

> . . . the lack of fiduciary duties imposed on ad hoc creditors' committees in CCAA proceedings could mean that they have less incentive (and no obligation) to be constructive participants in the proceedings . . .

[18] The changing constituency of ad hoc committee members, their fluctuating economic interests, and the uneven ability of committee members to access confidential information without risk of trading limitations create thorny ethical and practical issues for legal counsel appointed to represent the committees.

V. CONCLUSION

[19] Given the role of the Monitor, unsecured creditors committees will likely continue to be appointed on a case-specific basis in Canadian insolvency proceedings, rather than being the norm, and will likely continue to be scrutinized to determine whether they are necessary, cost-effective and conducive to advancing the restructuring. The experience of Canadian Courts to date with these committees has cast light on a number of issues, particularly of transparency and governance, that may have to be addressed in future proceedings.