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SALES OR PLANS: A COMPARATIVE ACCOUNT OF THE "NEW" CORPORATE REORGANIZATION

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In this article, Professors Stephanie Ben-Ishai and Stephen Lubben explore the recent surge in popularity of "quick sales", essentially the prereorganization sale of an insolvent debtor's assets. In their examination of quick sales, the authors use the recent examples of the General Motors, Chrysler, and Lehman Brothers insolvencies to illustrate the popularity and relevance of preplan sales. The authors then move on to a more detailed discussion of the quick-sales process in the United States and Canada, explaining the differences and similarities between both countries' regimes, and weighing the costs and benefits of each approach. Ultimately, the authors argue that elements of speed and certainty mark the biggest difference between the two jurisdictions, as the American approach offers greater flexibility, which is apt to facilitate quicker asset sales. However, Ben-Ishai and Lubben assert that the Canadian approach also provides significant benefits, particularly in the realm of employee protection and the ability of the monitor to act as an independent check on quick-sales proceedings. Accordingly, the authors conclude that while the American approach is advantageous in situations with exceptional time constraints, the Canadian approach under the *Companies Creditors' Arrangement Act* (CCAA) is more beneficial for a typical corporate reorganization, insofar as the role of the monitor and other limitations of the CCAA prevent overuse of the quick-sales process.

Cet article explore l'envolée des « ventes rapides », soit la vente des actifs d'un débiteur insolvable avant une réorganisation corporative. Aux fins de cet examen, les auteurs utilisent les exemples récents de General Motors, Chrysler, et Lehman Brothers pour souligner la popularité et la pertinence des ventes « préplan ». Les auteurs passent ensuite à une discussion plus détaillée du processus de ventes rapide aux États-Unis et au Canada, expliquant les différences et les similitudes entre les régimes des deux pays, et évaluant les avantages et les désavantages de chaque régime. Les auteurs font valoir que les éléments de vitesse et de sécurité marquent la plus grande différence entre les deux pays, et que l'approche américaine offre une plus grande flexibilité, ce qui est de nature à faciliter les ventes d'actifs plus rapidement. Toutefois, les auteurs affirment que l'approche canadienne offre également des avantages considérables, en particulier dans le domaine de la protection des employés et en ce qui concerne la capacité du moniteur à agir comme un contrôle indépendant sur les procédures de vente rapide. Les auteurs concluent donc que, bien que l'approche américaine est avantageuse dans des situations exceptionnelles qui comportent des contraintes de temps, l'approche canadienne en vertu de la *Loi sur les arrangements avec les créanciers des compagnies* (LACC) est plus bénéfique dans le contexte d'une réorganisation d'entreprise classique, dans la mesure où le rôle du moniteur et d'autres consignes de la LACC préviennent l'abus du processus de vente rapide.

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Introduction

Chrysler and General Motors Corporation (GM) recently completed reorganization proceedings to address their persistent financial and operational troubles.[1] Both have long, historic ties to the United States and Canada, dating back to the years before the Great War when Canadian McLaughlin Model F automobiles were sold with Buick engines. Both debtors were provided with sizeable governmental financing from Canada and the United States during their reorganizations,[2] and both cases involved a swift sale of the "good" parts of the debtors' assets, while what remained was left behind for liquidation.

Somewhat surprisingly, given both debtors' considerable presences in Canada, as well as the Canadian government's extensive involvement in the cases, neither GM nor Chrysler filed a *Companies' Creditors Arrangement Act* (CCAA) proceeding in Canada.[3] There was not even an attempt to have the US proceedings "recognized" in Canada. As far as Canadian creditors were concerned, GM and Chrysler were not really bankrupt.[4] Yet their assets—including those located in Canada—have been sold to new owners.

The tendency in the international literature is to focus on the polar extremes of the US corporate bankruptcy process—on the one side, long, traditional reorganization cases as were often seen in the 1980s, and on the other, extremely quick "prepacks", a term which has developed a wealth of meanings. The reality is, however, that many large Chapter 11 cases now involve asset sales.[5] In such cases, the bulk of the debtor's assets are sold in the early days of the case, and the remainder of the case is focused on deciding how to allocate the proceeds. Thus, despite some overheated commentary to the contrary, the Chrysler and GM cases were not all that remarkable.

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1 *Indiana State Police Pension Trust v Chrysler LLC* (*Trustee of*) (*sub nom Re Chrysler LLC*), 576 F (3d) 108, 2009 US App LEXIS 17441 (2d Cir 2009), vacated as moot, 130 S Ct 1015, 175 L Ed 2d 614 (2009) [*Indiana State Police Pension*]; *Re General Motors Corp*, 407 BR 463, 2009 Bankr LEXIS 1687 (Bankr SD NY 2009) [*General Motors* cited to BR].

2 In the case of Canada, financial assistance came from both the federal and provincial (Ontario) governments.

3 RSC 1985, c C-36 [*CCAA*].

4 With the possible exception that larger creditors doing business in the United States may have been subject to the US Bankruptcy Court's jurisdiction. See 11 USC § 362 (2006).

5 See e.g. Douglas G Baird & Robert K Rasmussen, "The End of Bankruptcy" (2002) 55:3 Stan L Rev 751; Stephen J Lubben, "The 'New and Improved' Chapter 11" (2005) 93:4 Ky LJ 839 [Lubben, "New and Improved"].

This article explores the question of why such an asset sale was not also pursued in Canada for these debtors. More generally, it examines the tools provided in the United States and Canada to sell assets in lieu of a more traditional reorganization process.

As we show, both the United States and Canada have well-established case law that supports the "preplan" sale of a debtor's assets. The key difference between the jurisdictions thus turns not on basic procedures, but rather on the broader context of those procedures. For example, although not without some controversy and conflict among decisions, it is generally possible to sell a debtor's assets free of any obligations or liabilities in the United States.[6] Indeed, the only obligations that survive such a sale are those that the buyer willingly accepts, and those that must survive to comply with the US Constitution's requirements of due process. In Canada, the debtor has less ability to "cleanse" assets through the sale process. Particularly with regard to employee claims, a preplan sale under the CCAA is not apt to be quite as "free and clear" as its American counterpart.

The jurisdictions also differ on the points at which the reorganization procedure can be invoked and the sale process commenced. Canada, like most other jurisdictions, has an insolvency prerequisite for commencing proceedings, whereas Chapter 11 does not. The Canadian sale process is tied to the oversight of cases by the monitor; without the monitor's consent, it is unlikely that a Canadian court would approve a preplan asset sale.[7] In the United States, on the other hand, there is no such requirement. Accordingly, a debtor can seek almost immediate approval of a sale upon filing. Finally, there remains some doubt and conflicting case law in Canada about the use of the CCAA in circumstances that amount to liquidation, particularly following an asset sale. In the United States, it is quite clear that Chapter 11 can be used for liquidation.[8]

We submit that these latter factors are the likely explanations for the failure to use the CCAA in the automotive cases. While authors have often noted specific differences between the US and Canadian asset sale processes, such as the use of competitive bids, we argue that it is the questions of speed and certainty that mark the biggest difference between the two jurisdictions, as the CCAA is sufficiently flexible to account for

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6 11 USC § 363(f) (2006).

7 See Jacob Ziegel, "The BIA and CCAA Interface" in Stephanie Ben-Ishai & Anthony Duggan, eds, *Canadian Bankruptcy & Insolvency Law: Bill C-55, Statute c47 and Beyond* (Markham, Ont: LexisNexis, 2007) 308 at 326-27.

8 See Stephen J Lubben, "Business Liquidation" (2007) 81:1 Am Bank LJ 65.

simple procedural differences. In the cases of GM and Chrysler, where the governments valued speed above all else, these issues came to the fore.

This paper begins with a summary of the relevant law in the United States, followed by an analysis of the Canadian law. We then engage in the true comparative work, noting both the similarities and the differences between the two systems and their approaches to preplan asset sales. We find that the US approach is more flexible and is thus apt to facilitate much quicker asset sales.

In Part II of the paper, our analysis concludes by considering the relative merits of the two approaches. The speed and flexibility of the US process is commendable in very large cases like those involving Lehman Brothers or GM, where the complexity of the business warrants a swift response. In these cases, the process is buttressed by the sophistication of the bankruptcy courts and the major creditor constituencies. Plainly, this flexibility would be less desirable in jurisdictions without the latter two features—another note of caution for those who would spread Chapter 11 (or the CCAA) across the globe.[9]

On the other hand, the virtually unbridled use of section 363 sales in the United States is not without its critics.[10] In particular, one of this article's authors has previously questioned if the current form of Chapter 11 cases benefits creditors—other than the secured creditors who typically demand the quick sale.[11] The CCAA avoids some of these concerns by protecting employees and interjecting the monitor as an independent voice in the proceedings.

In short, while we see the advantages of the Chapter 11 approach in exceptional times like those of the past two years, for a more typical corporate reorganization, the apparent limitations of the CCAA are not necessarily indicative of inefficiencies or points that should be changed. Instead, it is arguable that the monitor and other apparent "limitations" of the CCAA will prevent the overuse of the bankruptcy process by secured lenders who simply seek to foreclose on their collateral.

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9 See generally Stephen J Lubben, "Financial Distress and Emerging Markets" in Greg N Gregoriou, ed, *Emerging Markets: Performance, Analysis And Innovation* (Boca Raton, Fla: CRC Press, 2010) 635.

10 See Jay Lawrence Westbrook, "The Control of Wealth in Bankruptcy" (2004) 82:4 Tex L Rev 795.

11 See Lubben, "New and Improved", *supra* note 5 at 841-42.

I. Asset Sales Before Plans Compared

In this part, we examine the practice of quick sales in Canada as compared to the United States, and pinpoint the differences and similarities in how the Canadian system approaches preplan sales. The recently completed Canadian bankruptcy law reform process will undoubtedly influence the current law and practice around preplan sales in Canada. As we discuss in greater detail below, however, the changes will likely only further entrench the existing differences between the two jurisdictions and potentially unwind the increasing influence that the US approach has had on the Canadian system. This is not necessarily a negative outcome. In fact, the Canadian approach to quick sales may provide just the model that commentators critiquing the US approach taken in the bankruptcies of Lehman Brothers and Chrysler have been searching for.

A. The US Approach

In the United States, there are two ways for a corporate debtor to sell its assets. First, the debtor can propose the sale as part of a traditional reorganization plan.[12] Second, under section 363 of the US Bankruptcy Code, the debtor can sell its assets and then propose a liquidation plan that distributes the sale proceeds to creditors.[13] In the past ten to fifteen years, secured lenders have used the latter provision, plus the control inherent in being a secured lender (particularly the control that is present over the debtor's cash),[14] to take charge of Chapter 11 cases.[15] Among the well-known debtors that have used section 363 sales in their cases are TWA, Vlasic Foods, Polaroid, Bethlehem Steel, and most recently, Lehman Brothers.[16]

The preference for section 363 sales is driven by two factors: the speed of the process, which allows lenders to exit the proceeding before the debtor resolves all of its bankruptcy issues, and the ability under section

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12 See 11 USC § 1123(b)(4) (2006).

13 See John J Hurley, "Chapter 11 Alternative: Section 363 Sale of all of the Debtor's Assets Outside a Plan of Reorganization" (1984) 58:3 Am Bank LJ 233 at 240-41 (where the author noted more than twenty years ago that "it has become generally accepted that section 363(b) empowers a trustee or debtor in possession to sell all of the property of the debtor outside a plan of reorganization").

14 See Douglas G Baird & Robert K Rasmussen, "Private Debt and the Missing Lever of Corporate Governance" (2006) 154:5 U Pa L Rev 1209 at 1228-29.

15 Douglas G Baird & Robert K Rasmussen, "Chapter 11 at Twilight" (2003) 56:3 Stan L Rev 673 at 674-75 [Baird & Rasmussen, "Twilight"]. See also *Florida (Department of Revenue) v Piccadilly Cafeterias*, 128 S Ct 2326 at 2331, n 2, 171 L Ed 2d 203 (2008).

16 *C.f.* Lynn M LoPucki & Joseph W Doherty, "Bankruptcy Fire Sales" (2007) 106:1 Mich L Rev 1.

363 to sell assets "free and clear" of most claims. Indeed, with the possible exception of future tort claimants who could not know that they have claims, courts have ruled that section 363(f) provides very clean title to the debtor's assets.[17] As such, quick sales have become an increasingly popular outcome in large Chapter 11 cases, with approximately two-thirds of all large bankruptcy proceedings involving a sale of the firm, as opposed to a more traditional reorganization plan.[18]

A sale does little to change a creditor's recovery against the debtor, and thus a preplan sale is not formally subject to any of the rules associated with the confirmation of a plan.[19] Instead, creditors are provided with a variety of tools to protect against the threat of a "lowball" sale, including the ability to submit competing bids and credit bids in the case of secured creditors.[20]

In particular, if a debtor in possession elects to sell its assets in a section 363 sale, the process typically involves identifying an initial bidder, frequently called a "stalking horse", and approving the bidding procedures.[21] These bidding procedures provide structure for the solicitation of competing bids, followed by an auction if any competing bids materialize.[22] Bidding procedures can also include expense reimbursement and "breakup" or break fees for a stalking horse bidder that does not ultimately win the debtor's assets.[23] Once the sale is complete, the debtor either proceeds to formulate a Chapter 11 liquidating plan or converts the case to Chapter 7, in which case a trustee will conduct the liquidation.

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17 See especially *Re Trans World Airlines,* 322 F (3d) 283, US App LEXIS 4530 (3d Cir 2003); *General Motors*, *supra* note 1 at 505-506.

18 See Kenneth Ayotte & David A Skeel, Jr, "Bankruptcy or Bailouts?" (2010) 35:3 J Corp L 469 at 476.

19 See *Re Trans World Airlines,* 2001 WL 1820326 at para 57, 2001 Bankr LEXIS 980 (Bankr Del 2001).

20 See 11 USC § 363(k) (2006). See also Bruce A Markell, "Owners, Auctions, and Absolute Priority in Bankruptcy Reorganizations" (1991) 44:1 Stan L Rev 69 at 121-22.

21 See *Re O'Brien Environmental Energy*, 181 F (3d) 527 at 530, 1999 US App LEXIS 16652 (3d Cir 1999) [*O'Brien* cited to F (3d)].

22 See CR Bowles & John Egan, "The Sale of the Century or a Fraud on Creditors? The Fiduciary Duty of Trustees and Debtors in Possession Relating to the 'Sale' of a Debtor's Assets in Bankruptcy" (1998) 28:3 U Mem L Rev 781 at 805-36.

23 See e.g. *Re Reliant Energy Channelview LP*, 594 F (3d) 200, 2010 US App LEXIS 956 (3d Cir 2010) (please note, however, that the court in this case decided not to award the breakup fee to the prospective purchaser); Bruce A Markell, "The Case Against Breakup Fees in Bankruptcy" (1992) 66:4 Am Bank LJ 349 at 359. It should be noted that § 363 provides no textual basis for the approval of bidding procedures or breakup fees, but rather these tools have been developed by American bankruptcy courts as part of the exercise of their powers to approve non-ordinary course asset sales.

Aware of the risk that the terms of a sale might constrict a future plan and creditors' ability to vote on that plan, courts have developed rules that prevent the imposition of a reorganization plan through the sale process.[24] This is the so-called rule against "sub rosa" plans—that is, plans disguised as sales. While the rule is applicable across the United States, the content of the rule varies by judicial circuit.[25] In the Second Circuit, which includes the Southern District of New York (i.e., Manhattan), the rule only seems to preclude sale provisions that explicitly dictate the terms of a future plan or the initial distribution of the sale consideration.[26]

The automotive cases followed this basic structure. As Judge Gonzalez noted in *Re Chrysler LLC*, "The sale transaction ... is similar to that presented in other cases in which exigent circumstances warrant an expeditious sale of assets prior to confirmation of a plan. The fact that the US government is the primary source of funding does not alter the analysis under bankruptcy law."[27]

As noted, the desirability of this turn in American corporate bankruptcy cases is the subject of a good deal of debate.[28] There are concerns about the propriety of turning the bankruptcy court and Chapter 11 into a glorified foreclosure process, particularly if the cost of that process is not borne by secured lenders. Moreover, some recent studies suggest that secured lenders may be driven to embrace quick sales for reasons that have nothing to do with maximizing asset values.[29] This debate has often been clouded by skepticism over the strong empirical claims that Baird and Rassmussen, the first academics to fully describe the growth of section 363 sales, made in connection with their analysis of the issue.[30] Neverthe-

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24 See Jason Brege, "An Efficiency Model of Section 363(b) Sales", Note, (2006) 92:7 Va L Rev 1639 at 1650.

25 See James J White, "Death and Resurrection of Secured Credit" (2004) 12:1 Am Bankr Inst L Rev 139 at 161-63.

26 See e.g. *Re Westpoint Stevens*, 333 BR 30 at 52, 2005 US Dist LEXIS 28153 (SD NY 2005).

27 405 BR 84 at 87, 2009 Bankr LEXIS 1323 (Bankr SD NY 2009), aff'd *Indiana State Police Pension*, *supra* note 1.

28 See Westbrook, *supra* note 10.

29 See especially Sarah Pei Woo, "Simultaneous Distress of Residential Developers and Their Secured Lenders: An Analysis of Bankruptcy & Bank Regulation" (2010) 15:3 Fordham J Corp & Fin L 617.

30 See Lynn M LoPucki, "The Nature of the Bankrupt Firm: A Response to Baird and Rasmussen's *The End of Bankruptcy*" (2003) 56:3 Stan L Rev 645 at 653. In particular, Baird and Rasmussen have argued that "[s]mall businesses in Chapter 11 have little going-concern value, and sales are usually the best way to preserve whatever value exists" (Baird & Rasmussen, "Twilight", *supra* note 15 at 688).

less, as a descriptive matter, it is beyond debate that GM and Chrysler's sales represent a much larger trend.[31]

In Canada, the two courses of action open to an insolvent corporate debtor include reorganization under the CCAA[32] or reorganization under the *Bankruptcy and Insolvency Act*[33] (BIA). The CCAA is the main piece of legislation governing the restructuring of large corporations,[34] and is preferred in reorganizations where a court is dealing with matters that are novel or complex. As part of a reorganization under the CCAA, a preplan sale of a debtor's assets is an increasingly common practice in Canada. This is particularly the case where time is of the essence because the debtor will soon be unable to meet its operating expenses.[35]

Although the CCAA has been likened to Chapter 11 of the US Bankruptcy Code,[36] there are nevertheless important differences between the two statutes.[37] For example, the CCAA lacks the detailed statutory framework for quick sales provided by the US Bankruptcy Code.[38] This

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31 See e.g. Stephen J Lubben, "No Big Deal: The GM and Chrysler Cases in Context" (2009) 83:4 Am Bank LJ 531.

32 *Supra* note 3.

33 RSC 1985, c B-3 [*BIA*].

34 The CCAA was rarely used during the early twentieth century. During the recession years in the 1980s, however, "the CCAA was radically transformed from a largely dormant Act to a dynamic and judicially driven restructuring vehicle, albeit one without firm rules" (Jacob Ziegel, "Bill C-55 and Canada's Insolvency Law Reform Process" (2006) 43:1 Can Bus LJ 76 at 87).

35 See Sheryl E Seigel, "Distinctions with a Difference: Comparison of Restructurings Under the CCAA with Chapter 11 Law and Practice" (2010), online: McMillan <http://www.mcmillan.ca>.

36 Toronto attorney Terrence Dolan once noted that the CCAA is "like a Chapter 11 proceeding, with no rules" (Rick Haliechuk, "British Bankruptcy Law Takes Control from Firm", *The Toronto Star* (29 May 1992) B4). The CCAA has also been characterized as a "Canadian answer to Chapter 11 of the United States Bankruptcy Code" (Sean R Dargan, "The Emergence of Mechanisms for Cross-Border Insolvencies in Canadian Law" (2001) 17:1 Conn J Int'l L 107 at 112).

37 See Lynn M LoPucki & George G Triantis, "A Systems Approach to Comparing US and Canadian Reorganization of Financially Distressed Companies" (1994) 35:2 Harv Int'l LJ 267 at 268. The authors note:

> Though Canada shares a common language and heritage with the United States, it has rejected many legal doctrines thought to be fundamental to the operation of the U.S. system of bankruptcy reorganization, such as cram down, the estate, the debtor in possession, and the debtor's option to assume or reject executory contracts (*ibid*).

38 See Seigel, *supra* note 35. In this sense, the CCAA might be better compared with the receivership process used in the United States before the New Deal to reorganize insolvent railroads (see generally Stephen J Lubben, "Railroad Receiverships and Modern Bankruptcy Theory" (2004) 89:6 Cornell L Rev 1420).

difference continues to persist even with the recently enacted amendments, which are designed to provide a codification of practices and laws that have developed over the past two decades[39] and to lend more structure to the CCAA, which has been characterized by—and sometimes criticized for—its flexibility.[40] Amongst the recent amendments is the new section 36 of the CCAA, which dictates the rules for asset sales and the disposition of assets. The new provision lays out the specific factors to be considered in deciding whether the court should grant authorization for the sale and transfer of the debtor's assets.[41] However, these amendments do not delineate a detailed framework through which to conduct the sales process; rather, they merely outline relevant considerations for the court to weigh in approving the sale. Further, this list is not exhaustive.[42]

B. Sales Procedures and Protection for Purchasers Under the CCAA

The most significant difference between the Canadian and US approaches to quick sales is that the United States has a more established quick-sales process under section 363 of the US Bankruptcy Code. Although, like their American counterparts, Canadian courts do approve preplan sales and "make orders conveying title to the purchased assets free and clear of liens and encumbrances," the same structured sales procedures typically used in a Chapter 11 proceeding are not as common in Canada.[43] Rather, in the past, without any express provisions dealing with asset sales in the CCAA, Canadian courts relied on their powers to impose terms and conditions under a stay order,[44] and their inherent jurisdiction under the CCAA, to approve asset sales. However, the new section 36 has since been added to the CCAA in order to provide some guidance on how to approach asset sales in Canada.

As noted above, the quick-sales process under Chapter 11 often proceeds as follows: the debtor corporation

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39 See Andrew JF Kent et al, "Canadian Business Restructuring Law: When Should a Court Say 'No'?" (2008) 24:1 BFLR 1 at 2.

40 See Yaad Rotem, "Contemplating a Corporate Governance Model for Bankruptcy Reorganizations: Lessons from Canada" (2008) 3:1 Va L & Bus Rev 125 at 140 ("the CCAA has been acknowledged as a flexible restructuring tool that is administered by highly involved bankruptcy judges").

41 See Stephanie Ben-Ishai, *Bankruptcy Reforms: 2008* (Toronto: Thomson Carswell, 2008) at 59.

42 *Ibid*.

43 Seigel, *supra* note 35.

44 See *CCAA*, *supra* note 3, s 11.

> identifies a "stalking horse" or initial bidder, usually after a marketing process of some kind, and enters into a definitive agreement [with that bidder in order to sell] the company's assets, with the understanding that the agreement will be shopped around to other prospective purchasers, who will be solicited to top its deal.[45]

A US bankruptcy court—specialized in dealing with such matters[46]—is then asked to approve this stalking-horse bid, along with the auction date and bidding procedures, which set the rules of the auction. The bidding procedures will generally include built-in protections for the stalking horse, including minimum bidding increments, an approved form of purchase agreement for competing bids, standard bidder qualifications, a break fee[47] to be paid to the stalking horse if it is outbid, and some form of expense reimbursement for the stalking horse if it is outbid.[48]

Historically, the Canadian quick-sales process has not had these same procedures and protections. Rather, a Canadian quick-sale transaction may proceed as follows under the CCAA:

- (i) Submission of non-binding letters of intent or expressions of interest by prospective bidders;
- (ii) Due diligence;
- (iii) Submission of binding agreements and deposits by all bidders having decided to do so;
- (iv) Negotiations by the debtor or monitor with one or more interested parties (who are requested to put in their highest and best offers);
- (v) The selection of the preferred purchaser;
- (vi) An application to the court for approval of the proposed purchase agreement (which is often sealed and not made part of the public record); and

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45 Pam Huff, "Court-Supervised Mergers and Acquisitions Opportunities for Knowledgeable Buyers in Distressed Markets" (16 October 2007), online: Blakes <http://www.blakes.com>.

46 Unlike in Canada, where there are no specialized federal bankruptcy courts developing their own body of law.

47 Or breakup fee, as it is typically termed in the United States. US bankruptcy courts are "generally prepared to approve break fees in the range of one per cent to three per cent of the purchase price, although the practice is not without controversy" (Huff, *supra* note 45). However, others insist that break fees are necessary to protect the stalking horse and to ensure an attractive initial bid, as opposed to a discounted offer, which would set the baseline too low for a meaningful auction process. See also, *O'Brien*, *supra* note 21 at 533.

48 Huff notes that bidding incentives, such as overbid protections, are "reasonably required by the stalking horse to compensate it for its costs and the arguable disadvantage of coming forward to establish the transparent baseline for the auction process" (*supra* note 45).

(vii) Court approval of the purchase transaction (without any further auction or ability of a third-party bidder to make a higher or better offer, should their circumstances or knowledge change).[49]

Leading Canadian insolvency practitioner, Sheryl Seigel, notes that unlike the American process under section 363, "Stalking horse bids, break-up fees and other bid protections, detailed bidding and sale procedures ... and auctions are not the norm"[50] in Canada. Absent these procedures, particularly those geared towards protecting an initial bidder, it could be more difficult for Canadian debtors to benefit from the quick-sales process as they might have more difficulty attracting a favourable starting offer. Finding other bidders who are willing to top the initial offer in a significant way could therefore become more challenging.

In Canada, the fact that purchase agreements recommended to the court for approval are often not made public compounds the issues surrounding the lack of bid protection provided for under the CCAA. As such, prospective bidders are "rarely given the opportunity to submit a higher or better offer once a successful bidder has been recommended to the court."[51] Canadian practitioners often complain that it is less likely that there will be a competitive bidding process under the CCAA, in which competing bids drive the price of the business up, and the debtor receives the maximum value for his or her corporation.[52] Accordingly, when compared to the American regime under Chapter 11, there is a perception that this lack of protection for bidders and lack of transparency in the bidding process results in a quick-sales process that is far less efficient and generates fewer desirable offers.

C. The Role of the Monitor

A notable feature distinguishing the governance and reorganization process under the CCAA from Chapter 11 is the requirement to appoint a monitor. In CCAA cases, a monitor is appointed as an officer of the court in order to observe and report back to the court on the activities of the

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49 Seigel, *supra* note 35. The author also notes that "Canadian courts are reluctant to override a transaction recommended by the debtor and monitor, if the sales process followed is found to have fairness and integrity" (*ibid*).

50 *Ibid.*

51 *Ibid.*

52 This, in turn, maximizes the benefit for their creditors. Of course, it is arguable that the existence of competing bidders is more theoretical than real in the United States: see LoPucki & Doherty, *supra* note 16.

debtor.[53] The recent amendments to the CCAA seek to codify further the role of the monitor.

The mandatory appointment of a monitor is a relatively new requirement. Before 1997, the CCAA did not require the appointment of a monitor. Instead, "a practice developed of having the court appoint an accounting firm to perform an officially sanctioned role in the *CCAA* proceedings."[54] Today, an accounting firm assigned to act as monitor has likely served as the firm's auditor prior to the proceeding.[55] Although the strategy of appointing the corporation's auditor as monitor instead of an unrelated party has been controversial in Canada, there are advantages to this practice. Specifically, "the auditor knows the corporation inside and out, has already established working relationships with management, and is cheaper to employ than another accounting firm. The auditor can also utilize his knowledge of the firm to formulate a restructuring."[56] As discussed in greater detail below, this practice will change with the limits imposed on who can serve as a monitor under the new amendments to the CCAA.

The purpose of the monitor is to act "as a watchdog to observe the conduct of management and the operation of the business while a plan [is] being formulated."[57] In order to fulfill this role, monitors are typically "given express access to the debtor's books, records and property."[58] In the context of this watchdog position, "the frequency of reporting to the bankruptcy judge and to the parties participating in the proceeding is quite high. Bankruptcy judges regard the Monitor as their 'eyes and ears' in dealing with the debtor firm."[59] However, in the majority of cases, the monitor's role and influence extends beyond that of watchdog.[60] Indeed, while monitors can be appointed by the court, they can also be "hired by the debtor and in substance often act as an advisor to the debtor, albeit with special responsibilities."[61] Making the monitor's role even more difficult to define is the fact that it is simply not set in stone. Rather, as Yaad Rotem asserts, "Canada has allowed its bankruptcy judges to decide on a

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53 See Seigel, *supra* note 35.

54 Kent et al, *supra* note 39 at 13.

55 See Rotem, *supra* note 40 at 149.

56 *Ibid* at 149.

57 Kent et al, *supra* note 39 at 13.

58 *Ibid* at 14.

59 Rotem, *supra* note 40 at 144-45.

60 See *ibid*.

61 Kent et al, *supra* note 39 at 15.

case-by-case basis what precise role the court-appointed official should fulfill."[62]

The monitor's role can even be extended to include supervising or actively participating in a sales process.[63] Andrew Kent notes that "in their reports monitors now routinely go beyond simply providing information. They will express views and make recommendations to the court concerning matters before the court,"[64] including preplan sales. Indeed, Rotem states that monitors "examine restructuring proposals, purchasing offers from third parties, suggested sales of assets, appraisals of the firm, cash-flow projections made by the firm, and generally, any approach taken to dispose of the corporation's assets."[65]

The monitor's influence is particularly important in finalizing a quick sale under the CCAA. As quick sales are commercial transactions implemented "during the course of *CCAA* proceedings before a plan is filed,"[66] court approval is typically substituted for creditor approval. Kent writes:

> On application for approval of these transactions, invariably the monitor will file a report and make a recommendation as to whether the proposed transaction should be approved by the court. Almost as invariably, the courts will defer to the monitor's views. Accordingly, *in substance these transactions are really subject to monitor approval*. As a result the monitor's judgment has replaced the judgment of the court or the creditors.[67]

Monitors can use this substantial power to control a transaction. Kent asserts that monitors "can use the threat of withholding their approval to negotiate with the debtor."[68] Indeed, debtors know that "it will be difficult to obtain court approval for a major transaction without having the monitor's prior approval. So *the monitors can and do constructively influence the debtor's conduct*."[69] Kent goes so far as to state that it can "be the reality that the real negotiations in the proceedings take place in secret be-

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62 *Supra* note 40 at 141. While Rotem stresses that the role of the monitor can be difficult to pin down, he also notes that a monitor is *not* intended to manage the corporation on a daily basis (*ibid* at 142). In the United States, a similar phenomenon has developed with regard to "examiners", who by statute are appointed to investigate the debtor. Recent bankruptcy court decisions have instead used examiners to review fee applications and generally act as an all-purpose "neutral" in the case.

63 See Seigel, *supra* note 35.

64 Kent et al, *supra* note 39 at 16.

65 *Supra* note 40 at 145.

66 Kent et al, *supra* note 39 at 16-17.

67 *Ibid* at 17 [emphasis added].

68 *Ibid*.

69 *Ibid* [emphasis added].

tween the monitor and management for the debtor."[70] Accordingly, it is clear that the monitor plays a crucial role in the quick-sales process, as their approval can either "make or break" the transaction.

In contrast, there is no court-appointed monitor in Chapter 11 restructurings. As such, under Chapter 11, there is one less "hoop to jump through" in arranging a preplan sale, which can be very important in situations where time is of the essence (as is typically the case when an insolvent debtor is seeking a quick sale).

This Canadian hurdle may become more formal and difficult for a debtor corporation to surmount in the coming years. The 2009 amendments to the CCAA provided clarification on the role of the monitor that will take away some of the current flexibility that debtor corporations and the courts enjoy in defining the role. Specifically, the amended section 11.7 establishes that the court must appoint a monitor in CCAA proceedings, and that this person must be a trustee within the meaning of subsection 2(1) of the BIA.[71] Further, subsection 11.7(2) states that, except with express permission from the court, no trustee can be appointed as a monitor if they have during the preceding two years been a director, officer, or employee of the company, or related to the company in any way, even as an auditor or legal counsel.[72] Additionally, subsection 11.7(3) states that the court may replace the monitor following an application from a creditor if it considers that course of action appropriate.[73] Finally, all CCAA proceedings will be subject to the oversight of the Office of the Superintendent in Bankruptcy, and the monitor will be subject to the licensing and professional responsibility requirements that all licensed trustees are subject to in Canada.[74]

D. The Influence of the American Quick-Sales Process on Recent Canadian Proceedings

As discussed to this point, the quick-sales process under section 363 tends to have more formalized bidding and sales procedures and greater transparency than a traditional Canadian quick-sales process.[75] The monitor also adds an additional layer of non-judicial and non-creditor involvement that does not exist in the United States. The role of the moni-

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70 *Ibid*.

71 *Supra* note 3, s 11.7.

72 *Ibid*, s 11.7(2).

73 *Ibid*, s 11.7(3).

74 *Ibid*.

75 See Seigel, *supra* note 35.

tor has been quite flexible, however, and has changed with evolving CCAA practice. Both of these features may explain how the CCAA sales process has been influenced by the section 363 sales process in some recent CCAA filings.[76]

As a Canadian practitioner who regularly handles such files, Pam Huff notes that "there have been recent examples in Canadian insolvency proceedings where a stalking horse style process has been used from the outset or adopted later on in the process."[77] Huff stresses, however, that with "no statutory provisions to establish a stalking horse process at the beginning, there have been some purchasers and prospective purchasers who have complained that the process changed or migrated toward an auction, with the court entertaining the participation of late bidders."[78] This is problematic because if the rules are not clearly laid out at the beginning of the process, "the purchaser that thought it had the winning bid may not have negotiated protections, such as a break fee or expense reimbursement, which are typical in the U.S."[79]

It is unclear whether the Canadian quick-sales process benefits from only adopting certain elements of the American approach to quick sales, such as the stalking horse process, while not adopting other elements of the Chapter 11 regime—for example, break fees or other overbid protections. That is to say, simply borrowing bits and pieces from the section 363 process and trying to fit them into the less regimented Canadian model could result in confusion for both debtors and prospective purchasers. As such, it is worth examining Canadian cases in which elements of the section 363 process have been applied, and analyzing the impact this has had on the quick-sales process under the CCAA.

A major criticism of Canadian policy and research on the CCAA is the lack of comprehensive empirical databases similar to those long established in the United States. Comprehensive data currently does not exist on completed CCAA proceedings. There are several notable studies, however, including an analysis of recent cases under the CCAA conducted by Keith Pritchard.[80] Pritchard studied a total of seventy-nine CCAA cases taking place between September 1997 and August 2002. In his commentary, Pritchard reveals:

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76 Huff, *supra* note 45.

77 *Ibid.*

78 *Ibid.*

79 *Ibid.*

80 "Analysis of Recent Cases Under the Companies' Creditors Arrangement Act" (2004) 40:1 Can Bus LJ 116.

> Of the 29 successful filings, (a) three were identified as being both a pre-pack and a sale (10.3%), (b) seven were identified as being a sale only (24.0%), (c) six were identified as a pre-pack only (20.6%), (d) 11 were identified as neither a sale nor a pre-pack (37.8%), and (e) no information was reported for two of the cases (6.8%).[81]

Although these numbers indicate that both sales and prepacks may be slightly less popular in Canada than in the United States, Pritchard nevertheless notes that "sales and pre-packs represent a significant proportion of the successful cases."[82] Below, we analyze the two most notable of such cases and the cases that have followed them.

1. *Re Canadian Red Cross Society*

One aspect of the 1998 CCAA insolvency proceedings in *Re Canadian Red Cross Society*[83] dealt with a motion on the part of the Society (Red Cross) for the approval of the sale of its blood supply assets and operations.[84] The insolvency proceeding arose as a result of approximately $8 billion in tort claims that had been asserted against the Red Cross by victims of a "blood contamination problem that [had] haunted the Canadian blood system since at least the early 1980's."[85]

The court approved the sale of substantially all of the Red Cross's assets before any restructuring plan was ever put to creditors. The Red Cross obtained CCAA protection, and shortly thereafter, court approval of the sale and transfer of all of its blood supply assets and operations to two government agencies.[86] The court, however, stressed the social utility not only of the assets owned and controlled by the Red Cross, but that of their transfer as well. Specifically, in his decision, Justice Blair stated that the assets

> owned and controlled by the Red Cross are important to the continued viability of the blood supply operations, and to the seamless transfer of those operations in the interests of public health and safety. They also have value. In fact, they are the source of the principal value in the Red Cross's assets which might be available to sat-

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81 *Ibid* at 121.

82 *Ibid*.

83 *Re Canadian Red Cross Society/Société canadienne de la Croix-Rouge* (1998), 5 CBR (4th) 299 (available on WL Can) (Ont Ct J (Gen Div)) [*Canadian Red Cross*].

84 *Ibid* at para 3.

85 *Ibid* at para 2.

86 See Linc A Rogers, "CCAA Liquidations and Employment Issues" (Paper delivered at the Ontario Bar Association conference Building Bridges: Discussing Issues Affecting Labour in Insolvency Proceedings, 24 April 2009), online: Blakes <http://www.blakes.com>.

> isfy the claims of creditors. Their sale was therefore seen by those involved in attempting to structure a resolution to all of these ... social and personal problems.[87]

Accordingly, the court's emphasis on the social importance of approving this preplan sale indicates that Canadian courts may be more willing to approve a quick sale when there is some greater benefit to be obtained on top of simply repaying creditors. This is consistent with CCAA case law in general.

With respect to financial considerations, Justice Blair noted that the central question for determination was "whether the proposed Purchase Price for the Red Cross's blood supply related assets [was] fair and reasonable in the circumstances, and a price that is as close to the maximum as is reasonably likely to be obtained for such assets."[88] He noted that as long as the answer to that question is yes, then there is little quarrel as to the appropriateness of a preplan sale.[89] Specifically, he stressed that it does not matter to creditors and claimants "whether the source of their recovery is a pool of cash or a pool of real/personal/intangible assets. Indeed, it may well be advantageous to have the assets already crystallised into a cash fund."[90] As such, Justice Blair laid out some of the factors for consideration when approving a preplan sale and the rationale for such a decision.[91]

In *Fracmaster*,[92] Fracmaster, an Alberta corporation involved in restructuring under the CCAA, asked the court to approve the sale of substantially all its assets to UTI Energy. A syndicate of Fracmaster's creditors supported this application, but presented to the court the alternative plan of lifting the current stay on the proceedings and appointing the monitor as receiver and manager of Fracmaster. Although the syndicate

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87 *Canadian Red Cross*, *supra* note 83 at para 7.

88 *Ibid* at para 16.

89 *Ibid.*

90 *Ibid.*

91 The court's decision in *Canadian Red Cross* was followed in *Re Playdium Entertainment* (2001), 31 CBR (4th) 302 at para 11, 18 BLR (3d) 298 (Ont Sup Ct J) [*Playdium*]; *Re Fracmaster*, 1999 ABQB 379 at para 29, 245 AR 102 [*Fracmaster*]. It was also explained in *Re PSINet* (2001), 28 CBR (4th) 95 at para 5 (available on QL) (Ont Sup Ct J (Commercial List)) [*PSINet*]. Additionally, this decision was mentioned in 27 other cases, including *Re Skydome*, [1999] OJ No 1261 (QL) at para 6 (Ont Ct J (Gen Div) (Commercial List)); *UTI Energy v Fracmaster Ltd*, 1999 ABCA 178 at para 15, 244 AR 93; *Re T Eaton Co* (1999), 14 CBR (4th) 298 at para 4 (available on QL) (Ont Sup Ct J (Commercial List)); *Re Canadian Airlines*, 2000 ABQB 442 at para 173, 265 AR 20; *Re Redekop Properties*, 2001 BCSC 1892 at para 75, 40 CBR (5th) 62; *Re 843504 Alberta Ltd*, 2003 ABQB 1015 at para 15, 351 AR 222 [*843504 Alberta*].

92 *Fracmaster*, *supra* note 91.

supported the sale to UTI (it was contractually obliged to), it wanted the stay lifted and a receiver appointed so that it could proceed to enforce its security, even if the court declined to approve the UTI sale under the CCAA.

While the UTI sale would have been beneficial to secured creditors, it offered nothing in the way of compensation to unsecured creditors. To that end, several parties objected to both Fracmaster and the syndicate's applications. Specifically, two such parties, Mr. Balm and the Janus Corporation, "[applied] to continue the stay, adjourn the other applications, appoint an interim receiver, and have the court direct the calling of meetings for consideration of its proposal by the secured creditors, the unsecured creditors and the shareholders."[93] In addition, another corporation called Calfrac applied to purchase Fracmaster; its proposal made some small provisions for unsecured creditors.

In considering the applications at hand, the court was emphatic in its support of *Canadian Red Cross*, with Justice Paperny stating:

> I accept and support the broad statement made by Blair, J., in *Canadian Red Cross Society* (at p. 10):
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> "I cannot accept the submission that the court has no jurisdiction to make the order sought. The source of the authority is twofold: it is to be found in the power of the court to impose terms and conditions on the granting of a stay under s. 11; and it may be grounded upon the inherent jurisdiction of the court, not to make orders which contradict a statute, but to 'fill in the gaps in the legislation so as to give effect to the objects of the *CCAA*, including the survival program of a debtor until it can present a plan'."
>
> This statement must be read in light of the following wording (at p. 10):
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> *"It is very common in* CCAA *restructurings for the court to approve the sale and disposition of assets during the process and before the Plan is formally tendered and voted upon."*[94]

Despite this endorsement of the court's ability to authorize quick sales, however, Justice Paperny was less enthusiastic about the proposed transactions in this case. Noting that there was "no value in Fracmaster greater than the amount owed to the secured creditors,"[95] Justice Paperny questioned the ability of the Balm/Janus and Calfrac proposals to actually make provisions for unsecured creditors and shareholders. Specifically, Justice Paperny said that both proposals were, on their face, only "mar-

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[93] *Ibid* at para 3.

[94] *Ibid* at para 29 [emphasis added].

[95] *Ibid* at para 32.

ginally better for the unsecured creditors and, possibly, for the shareholders."[96]

Further, the Balm/Janus proposal contemplated a delay, which the court ruled was "significant in the circumstances."[97] Underscoring the substantial losses already faced by Fracmaster's creditors, the court noted that the "Balm/Janus proposal [put] the Syndicate ... at risk to lose even more."[98] In contrast, the "unsecured creditors and the shareholders face[d] no such risk if there [was] delay—they [had] only the possibility of recovering some amount greater than zero."[99] As such, the court did not approve the Balm/Janus application.

Similarly, the court asserted that the Calfrac proposal was "no more a plan than ... the UTI proposal. Although it slightly better[ed] UTI's pricing structure, it fail[ed] to contemplate practical procedures, including a provision for consultations with the stakeholders or a method of determining claims."[100] Accordingly, Calfrac's application was also rejected.

Concerning the main proposal in question—the UTI sale—Justice Paperny stated:

> It may well be that the UTI proposal is a commercially provident deal. The fact that it is not in the form of a plan is not in and of itself fatal in CCAA proceedings. However, the proposed transaction does not create a pool of cash in which unsecured creditors or shareholders can ultimately participate for their general benefit. It does not provide for the opportunity to consult with those stakeholders because it does not contemplate their receipt of any benefit. The court does not have the comfort of an independent opinion as to the fairness of the transaction or the process leading up to it. It has only a limited opportunity to evaluate the proposal. However reasonable the proposal may be, its purpose is to facilitate a sale for the benefit of the Syndicate. That can be accomplished in a different fashion without distorting the spirit of the CCAA. These concerns, cumulatively, lead me to no other conclusion than this proposed sale ought not to be approved under the CCAA.[101]

Finally, the court approved the secured creditors' application to have the stay lifted, and granted the request to have a monitor appointed as receiver and manager of the property and assets of Fracmaster. Justice Paperny declined only to direct the monitor to approve the UTI proposal,

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96 *Ibid*.

97 *Ibid* at para 35.

98 *Ibid*.

99 *Ibid*.

100 *Ibid* at para 37.

101 *Ibid* at para 40.

claiming that such an action would "fetter" the discretion of the monitor.[102]

The *Fracmaster* opinion stands in contrast to cases like *Chrysler* in the United States, where the debtor's assets were sold in a preplan sale that only benefited secured lenders and those unsecured creditors deemed sufficiently important for ongoing operations.[103] The *Fracmaster* opinion also directly addresses a key controversy in the United States: should a section 363 sale be used to benefit only secured creditors or should the latter be forced to run recourse to their statutory enforcement rights for priority repayment? While the Canadian case law is somewhat less developed than its US counterpart, *Fracmaster* shows that preplan asset sales in Canada—unlike in the United States—are not a complete substitute for traditional reorganizations. Rather, the use of a quick sale appears limited to those instances where the benefits will be shared throughout the debtor's capital structure. Indeed, where a range of the debtor's stakeholders share the benefits of a preplan asset sale, a single creditor of the debtor will not be able to veto the sale. This is highlighted in the next case we consider.

PSINet involved a joint hearing between the US Bankruptcy Court and the Superior Court of Justice of Ontario.[104] The hearing concerned the proposed sale of PSINet's assets in Canada to Telus Corporation. The assets in question were owned in part by the Canadian applicants under the CCAA filing and in part by their US parent company. The only objection to the sale came from the Royal Bank of Canada, who wished to be paid in full the balance of payments owing under several equipment leases. In response, PSINet proposed that the sale be "approved with the proviso vis-à-vis the Royal Bank that an amount of money for the full claim be set aside with ... PricewaterhouseCoopers Inc., the monitor in these proceedings, pending a further determination of entitlement."[105]

In its analysis, the Ontario court held that the bank would not be "prejudiced or otherwise disadvantaged by the arrangements proposed by the PSINet companies. To the contrary in this real time litigation situation, there would be material prejudice ... to the other stakeholders if the Telus transaction were not proceeded with."[106] In approving the sale, Justice Farley used *Canadian Red Cross* as support for his decision, stating that the latter case is evidence that "the court has jurisdiction to approve

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102 *Ibid* at para 44.

103 See *Indiana State Police Pension*, *supra* note 1.

104 *PSINet*, *supra* note 91.

105 *Ibid* at para 2.

106 *Ibid* at para 3.

a sale where circumstances dictate ... prior to a CCAA plan being submitted."[107]

2. *Re Consumers Packaging*

Re Consumers Packaging[108] was another recent CCAA case where asset sales played a large role. It was another instance where the sale of substantially all of the debtor's assets was approved by the court under the CCAA before creditors voted on a plan. In this case, Consumers Packaging Inc. (Consumers) had filed for protection under the CCAA in May 2000. KPMG was appointed monitor under section 11.7 of the CCAA. In June, Justice Farley authorized Consumers "through an Independent Restructuring Committee and its Chief Restructuring Officer to fix a date upon which interested third parties were to submit firm, fully financed offers to purchase all or any part of Consumers' business."[109] The restructuring committee, its chief officer, and the monitor agreed on a preferred bid and the sale approval motion was heard on 31 August.

In approving the sale, Justice Farley noted "as a fact that Consumers was 'quite sick' and 'financially fragile'."[110] He also stressed that the lenders who were supporting Consumers were threatening to withdraw if they were not paid out immediately. In so doing, Justice Farley underscored the usefulness of a preplan sale in cases where the situation of the debtor is quite desperate, and a timely solution is needed in the place of the more traditional, yet lengthy restructuring.

Justice Farley's sale approval order was appealed by an unsuccessful bidder, at which time the Ontario Court of Appeal stressed the validity of CCAA sales as a legitimate purpose of the statute. The Court of Appeal noted that the bid approved by Justice Farley "was the result of a fair and open process developed by Consumers and its professional advisors."[111] The court added that the successful bid provided more cash to creditors, had the least completing risk,[112] was not conditional on financing, was likely to close in a reasonable period of time, and would result in the continuation of Consumers' business and the retention of many of their em-

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107 *Ibid* at para 5.

108 (2001), 27 CBR (4th) 197, 150 OAC 384 (Ont CA) [*Consumers Packaging* cited to CBR], refusing leave to appeal from 27 CBR (4th) 194 (Ont SCJ (Commercial List)).

109 *Ibid* at para 2.

110 *Ibid*.

111 *Ibid* at para 3.

112 That is, risk of not closing the sale.

ployees.[113] Concerning the unsuccessful bidder, the court asserted that it was "the unanimous view of the Monitor, Consumers' Independent Restructuring Committee and Consumers' Chief Restructuring Officer that Ardagh's [unsuccessful] proposals were not viable and would, if pursued, result in the liquidation of Consumers, resulting in lower return to creditors, loss of jobs and cessation of business operations."[114] Here, the Court of Appeal outlined several key factors in pursuing a successful quick sale: the approval of the monitor, the approval of other key stakeholders, a fair bidding process, and a successful bid that maximizes creditors' returns and maintains the efficiency of the sales process.

The Court of Appeal's general reluctance to grant leave to appeal in such situations was also of note in this decision. The court noted that the

> authorities are clear that, due to the nature of CCAA proceedings, leave to appeal from orders made in the course of such proceedings should be granted sparingly. Leave to appeal should not be granted where, as in the present case, granting leave would be prejudicial to ... stakeholders as a whole, and hence would be contrary to the spirit and objectives of the CCAA.[115]

The court stressed that this was the case with Consumers, as there was a "real and substantial risk that granting leave to appeal ... [would] result in significant prejudice to Consumers and its stakeholders, in light of the significant time and financial constraints."[116] Accordingly, it appears that for an appeal on a quick sale to be successful, the appellant would need to demonstrate that the proposed sale is clearly against the interests of the debtor corporation and its creditors, and that greater harm would result from the sale than from preventing it. This is a significant burden of proof for an appellant to meet,[117] and represents a kind of

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113 See *Consumers Packaging*, *supra* note 108 at para 3.

114 *Ibid* at para 4.

115 *Ibid* at para 5 [footnotes omitted].

116 *Ibid.*

117 *Consumers Packaging* has been mentioned in six subsequent cases. It received neutral treatment in *Re Nortel Networks* (2009), 55 CBR (5th) 229 at para 33 (available on QL) (Ont Sup Ct J (Commercial List)) [*Nortel*]; *Re Railpower Technologies*, 2009 QCCS 2885 at para 105 (available on QL) [*Railpower Technologies*]; *Re Papiers Gaspésia*, [2004] JQ No 11951 (QL) at para 73 (Qc Sup Ct). The decision in *Consumers Packaging* was distinguished in *843504 Alberta*, *supra* note 91 at para 25; *Re Air Canada* (2003), 66 OR (3d) 257 at para 25, 174 OAC 201 (Ont CA). *Consumers Packaging* was affirmed in *Re Country Style Food Services* (2002), 158 OAC 30 at para 15 (available on QL) (Ont CA) [*Country Style Food*].

judicial protection for insolvency sales like that found in the United States' section 363(m).[118]

The recent case of *Nortel* involved a cross-border insolvency: Nortel, the applicant, was involved in insolvency proceedings in four countries.[119] In Canada, Nortel had been granted CCAA protection and proposed to maximize the value of the corporation through a quick sale.[120] This proposal was approved by the monitor. In June 2009, Justice Morawetz approved the Asset Sale Agreement between Nortel, as the sellers, and Nokia Siemens, as the buyers. Justice Morawetz also accepted Nortel's motion for approval of a stalking horse bidding process, utilizing such bidder protections as break-up fees and expense reimbursement.[121] Under this sale agreement, the purchaser was to assume both assets and liabilities. Moreover, this process involved no formal plan for compromise with creditors.

In granting Nortel's motion, the court discussed the applicant's main submissions, namely that "CCAA courts have repeatedly noted that the purpose of the CCAA is to preserve the benefit of a going concern business for all stakeholders, or 'the whole economic community'."[122] Furthermore, the "purpose of the CCAA is to facilitate arrangements that might avoid liquidation of the company and allow it to continue in business to the benefit of the whole economic community, including the shareholders, the creditors (both secured and unsecured) and the employees."[123] The court cited *Consumers Packaging* as authority for that statement.

In *Railpower Technologies*,[124] Railpower, a corporation that had already filed under the CCAA, brought a motion requesting authorization to sell substantially all of its assets to RJ Corman Railroad Group (RJ Corman), a Kentucky-based limited liability company. While Railpower's

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[118] 11 USC § 363(m) (2006):

> The reversal or modification on appeal of an authorization under subsection (b) or (c) of this section of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal.

[119] See *Nortel*, *supra* note 117.

[120] Specifically, Nortel argued that a quick sale was the best way to preserve jobs and company value (see *ibid* at para 10).

[121] *Ibid* at paras 1-2.

[122] *Ibid* at para 33.

[123] *Ibid* [footnotes omitted].

[124] *Supra* note 117.

most important creditor, the Ontario Teacher's Pension Plan Board, supported the motion, Progress Rail Services Corporation (Progress) contested the sale.

Specifically, Progress alleged that "the bidding process through which RJ Corman's bid was accepted was defective and prejudiced its rights. According to Progress, the offer that was finally accepted by Railpower's board of directors [was] less favourable to the creditors and other stakeholders in Railpower than would otherwise have been possible."[125] In its contestation, Progress therefore filed a new bid and requested that the court refuse to ratify the sale of Railpower's assets to RJ Corman, declare null and void any agreement between RJ Corman and Railpower, and reopen the bidding process in order to allow Progress to bid on Railpower's assets.

In denying Progress's motion contesting the sale of Railpower to RJ Corman, Justice Alary held that the sales process to which Progress objected was fair, and that the monitor had acted reasonably in accepting RJ Corman's bid. The court stressed that the bidding process

> included identifying and approaching qualified strategic partners or investors, making a data room available and signing Confidentiality Agreements. [In doing so,] Railpower ... and the Monitor asked for bids, requested details and additional information and kept the Board of directors informed.[126]

Furthermore, the monitor and Railpower awarded all potential investors equal chances to make their offers.

Citing *Consumers Packaging*, the court noted that "[t]here are authorities to the effect that courts have jurisdiction to authorize a sale of assets in CCAA proceedings in appropriate circumstances."[127] The court further noted that

> the CCAA has a broad remedial purpose and is aimed at avoiding the social and economic consequences of a termination of business operation and at allowing the corporation to carry out business, causing the least possible harm to employees and the communities in which it operates.
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> ...

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[125] *Ibid* at para 5.

[126] *Ibid* at para 90.

[127] *Ibid* at para 105 [footnotes omitted].

> According to the Monitor, a transaction with RJ Corman will allow Railpower's business to continue, as a going concern, although in a different form and under a new corporate identity.[128]

Lastly, the court also stressed that in authorizing the sale of assets under CCAA proceedings, substantial deference should be given to the monitor's recommendation "where the latter has acted reasonably."[129]

In *843504 Alberta*,[130] EdgeStone Capital Mezzanine Fund II Ltd. (EdgeStone)—a creditor of 843504 Alberta (Skyreach)—and the monitor of Skyreach sought an extension of the stay of proceedings granted under an initial order pursuant to the CCAA.[131] Through this extension, EdgeStone and the monitor intended to "establish a process for soliciting offers to purchase assets."[132] With the exception of GE Commercial Distribution Finance Canada (GE), Skyreach's creditors opposed the extension of the stay.

In this case, several parties used *Consumers Packaging* to argue in favour of the "sale of Skyreach's assets, either hard assets or shares, well before a plan is developed and presented to the creditors."[133] Specifically, the "Monitor, EdgeStone and GE [urged] that this process [would] maximize recoveries for the stakeholders, contending that the marketplace can best determine value of the debtor's assets," with EdgeStone relying on *Consumers Packaging* as authority.[134]

While Justice Topolniski did agree to extend the stay of proceedings, she did not endorse a preplan sale of Skyreach's assets. Rather, she asserted:

> I accept that the need for flexibility in CCAA proceedings may, in the appropriate circumstances, warrant a sale of a significant portion of a debtor's assets or undertaking before a plan of arrangement is put to the creditors. Obviously, each case must be assessed on its own unique facts, but in this case *there is no evidence that it is either necessary or in the stakeholders' best interests*. Accordingly, at this stage the proposed process is unacceptable.[135]

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[128] *Ibid* at paras 106-108, citing Janis P Sarra, *Rescue! The Companies' Creditors Arrangement Act* (Toronto: Thomson Carswell, 2007) at 9.

[129] *Railpower Technologies*, *supra* note 117 at para 93.

[130] S*upra* note 91.

[131] See *ibid* at para 1.

[132] *Ibid* at para 11.

[133] *Ibid* at paras 24-25.

[134] *Ibid* at para 25.

[135] *Ibid* at para 29 [emphasis added, footnotes omitted].

In her decision, Justice Topolniski distinguished the case at hand from *Consumers Packaging*, stating that in *Consumers Packaging*

> the court approved a going concern sale before the plan of arrangement was presented because the sale would preserve the business, albeit under new ownership, and because of uncertainty over whether the debtor could continue operations given its financiers' demands.[136]

Justice Topolniski felt that this was not the case in Skyreach's situation, however, and held that a preplan asset sale would not be beneficial.

E. Reforms to the CCAA: Codification of the Quick-Sale Approval Process

To a certain extent, the 2009 reforms to the CCAA codify and give greater certainty to the sale process and to the role of the monitor. Together with the case law that demonstrates a clear American influence on the CCAA quick-sale process, these reforms might indicate the increasing popularity of this approach. The reforms, however, remain uncertain in their application, do not introduce specific features for the process (such as break fees), and introduce greater obligations relating to employees, which will likely mean that we will not see a significant departure from the current process. That is, the Canadian quick-sale process will continue to be driven by the courts' concern with whether the sale is necessary and in the best interests of a broad range of stakeholders. The monitor will continue to be the guiding force for the court in making such a determination. There will continue to be a greater measure of unpredictability regarding the approval of a quick sale, as compared to the American process.

The new section 36 of the CCAA provides that a debtor company may not sell or dispose of its assets (outside of the ordinary course of business) during the administrative period in a CCAA restructuring, without court approval and notice to secured creditors who are likely to be affected by the proposed disposition. The court is required to consider specific enumerated factors in reaching a decision on the sale or disposition:

- Whether the process leading to the proposed sale or disposition was reasonable in the circumstances.
- Whether the trustee or monitor approved the process leading to the proposed sale or disposition.
- Whether the trustee or the monitor filed with the court a report stating that, in their opinion, the sale or disposition would be more beneficial to the creditors than a sale or disposition under a bankruptcy.

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[136] *Ibid* at para 27.

- The extent to which the creditors were consulted.
- The effects of the proposed sale or disposition on the creditors and other interested parties.
- Whether the consideration to be received for the assets is reasonable and fair, taking into account their market value.[137]

In addition to these factors, if the proposed sale or disposition is to a person who is related to the company, the court may only grant authorization if it is satisfied that

- good faith efforts were made to sell or otherwise dispose of the assets to persons who are not related to the company; and
- the consideration to be received is superior to the consideration that would be received under any other offer made in accordance with the process leading to the proposed sale or disposition.[138]

Despite any requirement for shareholder approval, including one under federal or provincial law, the court may authorize the sale or disposition even if shareholder approval was not obtained. Furthermore, the court may authorize the sale of assets free and clear.[139] As will be discussed in greater detail below, "free and clear" in the Canadian context has a different meaning than in the United States, and functionally means "subject to certain employee and Crown claims."

As a rationale for these reforms, Industry Canada indicates that the "reform is intended to provide the debtor company with greater flexibility in dealing with its property while limiting the possibility of abuse."[140] In particular, the factors introduced in the reforms are intended to provide the courts with legislative guidance and to provide the debtor company with direction. Industry Canada indicates that the amendments should improve the consistency of judicial decisions.[141] In addition, Industry Canada notes that the amendment that

> provides that a court may order that the property be sold to the purchaser free and clear of charges, liens and restrictions ... will increase the value of the property thereby creating greater wealth for the estate while also increasing the likelihood that property will be returned to productive use quickly.[142]

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137 See *CCAA*, *supra* note 3, s 36(3).

138 *Ibid*, s 36(4).

139 See *ibid*, s 36(6).

140 Industry Canada, "Corporate and Insolvency Law Policy – CCAA: Sales of Assets", online: Industry Canada <http://www.ic.gc.ca/eic/site/cilp-pdci.nsf/eng/cl00828.html>.

141 *Ibid*.

142 *Ibid*.

While the clear articulation of factors relating to the monitor's role in this process and the court's approval process, in addition to the explicit indication that assets can be sold free and clear appear to create a more transparent and bidder-friendly process, it will still remain a judicially-driven process that relies on the monitor's judgment and a significant degree of judicial discretion. In addition, a final restriction on the approval process for quick sales in a CCAA proceeding will continue to differentiate it from the American process: under subsections 5(a) and (b) of the CCAA, a court can only grant authorization for a quick sale of assets if it is satisfied that the company can and will make payments to its employees and former employees, immediately after court approval of the proposal. The payments must be equal to the amounts that the employees would be entitled to receive under paragraph 136(1)(d) of the BIA, if the employer became bankrupt on the date of the filing of the notice of intention (or that of the proposal if no notice of intention was filed). The employer must also pay wages, salaries, commissions, or compensation for services rendered after the proceedings commence and before the court approves the proposal. Finally, in the case of travelling salesmen, disbursements properly incurred by those salesmen in and about the bankrupt's business during the same period must be paid.[143]

It is worth noting that the CCAA provides employees with other protections as well. With regard to pension plans, if a company "participates in a prescribed pension plan for the benefit of its employees, the court may sanction a compromise or an arrangement in respect of the company only if"[144] certain requirements are satisfied. The compromise or arrangement has to provide for the payment of "an amount equal to the sum of all amounts that were deducted from the employees' remuneration for payment to the fund."[145] Furthermore, if the prescribed fund is regulated by an Act of Parliament, the situation must be arranged so that there is payment of "an amount equal to the normal cost, within the meaning of subsection 2(1) of the *Pension Benefits Standards Regulations, 1985*, that was required to be paid by the employer to the fund"[146] and "an amount equal to the sum of all amounts that were required to be paid by the employer to the fund under a defined contribution provision, within the meaning of subsection 2(1) of the *Pension Benefits Standards Act, 1985*."[147] In the case that the pension plan is any other prescribed pension plan, payment must be "equal to the amount that would be the normal

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143 See *BIA*, *supra* note 33, s 60(1.3)(a).

144 *CCAA*, *supra* note 3, s 6(6).

145 *Ibid*, s 6(6)(a)(i).

146 *Ibid*, s 6(6)(a)(ii)(A).

147 *Ibid*, s 6(6)(a)(ii)(B).

cost, within the meaning of subsection 2(1) of the *Pension Benefits Standards Regulations, 1985*, that the employer would be required to pay to the fund if the prescribed plan were regulated by an Act of Parliament,"[148] and must also include "an amount equal to the sum of all amounts that would have been required to be paid by the employer to the fund under a defined contribution provision, within the meaning of subsection 2(1) of the *Pension Benefits Standards Act, 1985*, if the prescribed plan were regulated by an Act of Parliament."[149] Naturally, the court has to be satisfied the company can and will make the aforementioned payments.[150]

Pension plan protections, however, are not as rigid as other employee-related protections. Section 7 of the CCAA provides for exceptions to the payment requirements just mentioned where "the relevant parties have entered into an agreement, approved by the relevant pension regulator, respecting the payment of those amounts."[151]

Under the CCAA, employees are perhaps most vulnerable when it comes to the preservation of their collective agreements. Where a debtor company cannot get its employees to agree to new collective agreement terms voluntarily, it can file for a notice to bargain "under the laws of the jurisdiction governing collective bargaining between the company and the bargaining agent."[152] There are, however, conditions that must be present in order for the court to issue an order authorizing the company to serve a notice to bargain. The conditions are: (a) a viable compromise or arrangement could not be made in respect of the company, taking into account the terms of the collective agreement; (b) the company has made good faith efforts to renegotiate the provisions of the collective agreement; and (c) a failure to issue the order is likely to result in irreparable damage to the company.[153] Nevertheless, it is clear that when these conditions are met, employees may be cornered into collective agreement terms that are less favourable than the ones to which they were prepared to agree initially. Having said that, it bears mentioning that the CCAA sections permitting the issuance of an order that authorizes the company to serve a notice to bargain do not address the potential eventuality of an impasse in negotiations. The CCAA contains no provisions giving the final say to one constituency or another; in fact, the court cannot impose new collective

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148 *Ibid*, s 6(6)(a)(iii)(A).

149 *Ibid*, s 6(6)(a)(iii)(B).

150 See *ibid*, s 6(6)(b).

151 *Ibid*, s 7.

152 *Ibid*, s 33(1).

153 *Ibid*, ss 33(3)(a)-(c).

agreement terms at all. Ian Klaiman[154] proposes interest arbitration as a solution to this problem; however, further discussion on this point is beyond the scope of this paper.[155]

II. The Costs and Benefits of Flexibility

As Part I has shown, both the United States and Canada share a common belief that it is permissible to sell a debtor's assets as part of a reorganization procedure. But upon closer inspection, it is clear that the US approach to asset sales is substantially broader—encompassing both a broader range of cases, and selling assets free from a broader range of claims. In this part, we examine the costs and benefits of this extra flexibility. We ultimately conclude that while section 363 in its fullest form is more beneficial for once-in-a-lifetime cases like that of Lehman Brothers, the more confined Canadian approach provides better safeguards against potential abuses of the reorganization process for the broader run of cases.

A. The Costs of Preplan Sales

In its purest form, a preplan sale of a debtor's assets would represent nothing more than a change of form, converting hard assets into cash for distribution to creditors. Such a sale could never be objectionable.

But reality is often somewhat different. Valuation of a corporation and its prospects is an inherently uncertain endeavour.[156] In most cases, it cannot be known what the present value of the debtor really is, and thus comparison to the proposed sale proceeds becomes rather speculative. Secured creditors can be expected to engage in excessively pessimistic valuations; unsecured creditors and shareholders will tilt in the opposite direction, leaving the judge to divine the true value.

This creates a risk of the manipulation of the bankruptcy process, a risk that we argue is more extreme in the United States because courts will now allow a section 363 sale to replace a plan in almost every case. For example, it remains conceivable that would-be objectors to a lowball

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[154] "Chapter c 47, Opening But Not Resolving Collective Bargaining: A Proposal for Mandatory Arbitration on Negotiation Impasse" (2010) 26:1 BFLR 135 (Klaiman also makes a more detailed comparison of the Canadian situation with the American one under § 1113 of the US Bankruptcy Code).

[155] For a more detailed critique of Canada's current insolvency reform process, see Jacob Ziegel, "Canada's Dysfunctional Insolvency Reform Process and the Search for Solutions" (2010) 26:1 BFLR 63 at 80 (this article also critiques the lack of power granted to the court when it comes to varying the terms of collective agreements).

[156] Sabin Willett, "*Gheewalla* and the Director's Dilemma" (2009) 64:4 Bus Law 1087 at 1096.

section 363 might be satisfied by side payments from either the purchaser or the debtor. If the senior lender is paid in full, it has no reason to object to an arrangement that might lead to a quicker realization of its recovery. If these side payments are funded by reduced value going into the estate, the problem is a significant threat to the bankruptcy process and to the basic premise of creditor equality.

The actual occurrence of such collusion is hard to detect. While many commentators alleged that such deals took place in the automotive cases—in particular with regard to the payments made to the unions—it is not at all clear that these arguments were not just reflections of the overheated political rhetoric surrounding the cases. Moreover, many of the claims seemed to amount, at heart, to an argument that the government should prefer investors over unions.[157] Given that the union was making significant labour concessions to the buyers of the automotive assets, a plausible argument can be made that the value the unions received was on account of their deal with the purchaser, and not as a result of their parallel status as unsecured creditors of the debtors.

In addition, even without strategic behaviour among parties, there remains the question of whether it is appropriate to conduct a reorganization proceeding for the sole benefit of a secured creditor. This quandary is especially acute in the United States, where the broad reach of section 363(f) means that the costs of some asset sales—including those in the two recent automotive cases—are borne by tort and other involuntary creditors. Specifically, since section 363(f) allows for the sale of assets free of these liabilities, the sale represents a transfer of value from these involuntary creditors to the debtor and, most often, its senior creditors.[158]

More broadly, there are important policy considerations embedded in the decision to allow a corporate reorganization scheme to transform into a kind of supercharged foreclosure mechanism, particularly if secured lenders are thereby able to avoid incurring costs that they would normally absorb in a state or provincial debt collection action.

B. The Benefits of Preplan Sales

The most obvious instance where preplan sales provide real benefits is a case where the debtor has going-concern value, but is unlikely to survive long enough to complete a formal reorganization process. *Lehman Broth-*

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157 See Ann Woolner, "Chrysler Mows Down Debtholders' Claims in Court" (5 June 2009), online: Bloomberg <http://www.bloomberg.com>.

158 More precisely, the cost of the § 363 sale in this situation is the marginal difference between a sale and a formal reorganization plan. For example, if the sale achieves something that could not be achieved under a plan, it represents a cost.

ers may offer an example of this: the court was presented with testimony that a failure to sell Lehman Brothers' key assets would result in a worldwide financial panic, with obvious consequences for the value of Lehman Brothers.[159]

Using a sale also allows the resolution of the debtor's financial distress to proceed, even in the face of disputes between creditors about payment and priority. The debtor's assets can be disengaged from the claims resolution process, allowing the business to resume normal operations in a swift manner that does not depend on the pace of the bankruptcy process. Moreover, it may be that claims are resolved faster if dissenting creditors lose their ability to obstruct the debtor's reorganization.

All of this has to be tempered by the realization that secured lenders can create an emergency at will simply by freezing the debtor's access to the cash needed for daily operations. A secured creditor with liens on all of the debtor's assets, including the debtor's operating cash, has the option to set a timetable for the bankruptcy case that will preclude any other option than a quick sale. The growth of secured financing—driven in part by the ability to sell "pieces" of a secured debt facility—means that more debtors will enter bankruptcy with strong controlling creditors (or groups of creditors) that may have the ability to trigger a sale.

C. Balancing

As previously discussed, the necessity of receiving the monitor's approval for an asset sale in Canada can impede the quick-sales process; however, the key role played by the monitor can also be framed in more positive terms, as the monitor helps to provide an independent assessment as to whether or not a quick sale is truly beneficial. Indeed, the recent amendments to the CCAA both emphasize and ensure the monitor's role as an independent advisor throughout the reorganization process. For example, subsection 11.7(2) states that, except with permission from the court, no trustee can be appointed as a monitor if they have been a director, officer, or employee of the company, or related to the company in any way (even as an auditor or legal counsel), during the preceding two

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159 *Re Lehman Brothers Holdings*, 433 BR 101, 2010 Bankr LEXIS 1260 (Bankr SD NY 2010) [*Lehman Brothers*] (Oral argument), online: Lehman Creditors' Committee <http://www.lehmancreditors.com>. Counsel for the debtor noted that "[a]ny failure to consummate [the Barclay's sale] may potentially cause a major shock to the financial system" (*ibid* at 146). Judge Peck remarked that "in unrebutted testimony [Mr Ridings, Lehman's investment banker] indicated through the proffer that the markets, in effect, would tank [if the sale was not approved]" (*ibid* at 171). See also Stephen Lubben, "The Sale of the Century and Its Impact on Asset Securitization: *Lehman Brothers*" (2009) 27:10 Am Bankr Inst J 1 at 1, n 4.

years.[160] This differs from the previous guidelines (or lack thereof) in the CCAA, under which the monitor was frequently someone who had acted in an auditing capacity for the company in question.

Moreover, under the recent amendments, the monitor must now be a trustee within the meaning of subsection 2(1) of the BIA.[161] As such, insolvency practitioners acting as monitors are now subject to additional oversight mechanisms from professional bodies, such as the Canadian Association of Insolvency and Restructuring Professionals (CAIRP), as well as the Office of the Superintendent of Bankruptcy (OSB). Accordingly, CAIRP and the OSB are available to oversee the activities of the monitor and to ensure that the monitor is acting as an independent advisor during the restructuring and reorganization process. Similarly, the new subsection 11.7(3) of the CCAA allows the court to replace the monitor following an application from a creditor, if it considers that course of action appropriate.[162] Therefore, if the monitor is not acting independently throughout the process, the court is equipped with the ability to appoint a new monitor. It remains to be seen how effectively CAIRP, the OSB and the courts will play their new role in "overseeing the overseer".

In its newly cemented position as an independent advisor, the monitor has the potential to play an important role during the quick-sales process, balancing the interests of the insolvent corporation with those of the creditors and other stakeholders. As Kent notes, the monitor is "[o]ne possible counterweight to the powers given to the debtor under the Canadian system."[163] The monitor also provides a possible check on an overreaching secured creditor, especially in situations where the debtor is unable or unwilling to resist the creditor's demands.

In acting as a "watchdog" throughout the CCAA process, the monitor has access to the debtor's books, records, and property.[164] As such, the monitor is extremely well positioned to provide an objective analysis of whether a quick sale is truly the best course of action, or whether the debtor would be likely to receive better returns for creditors by pursuing a more traditional reorganization. The monitor is not only obliged to weigh whether the debtor would be better off pursuing a traditional reorganization, but is also required to advise the court if declaring bankruptcy under the BIA would be a better option.[165] In so doing, the monitor is able to bal-

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160 *CCAA*, *supra* note 3, s 11.7(2).

161 *Ibid*, s 11.7(1).

162 *Ibid*, s 11.7(3).

163 Kent et al, *supra* note 39 at 13.

164 *Ibid* at 14.

165 *Ibid*.

ance the needs of the debtor with those of creditors, while also providing a check on the unbridled use of quick sales in Canada.

This role of the monitor—as an independent overseer, capable of balancing the interests of all parties—is consistent with the legislative goals of having a monitor in the first place. Indeed, during the 1997 round of legislative reform, the Bankruptcy and Insolvency Advisory Committee (BIAC), a task force appointed to study changes to the CCAA and BIA, stressed that the appointment of a monitor should be made mandatory in order to provide "creditors in *CCAA* applications [with] the same protection of a *professional and impartial* 'watchdog.'"[166] Similarly, in *Re United Used Auto & Truck Parts Ltd.*,[167] the court also stressed the balancing role that the monitor can play during the CCAA process. Here, the court asserted that the monitor has an "obligation to act independently and to consider the interests of the Petitioners and its creditors."[168] Accordingly, although satisfying the monitor that a quick sale is truly the best course of action places a significant burden on a Canadian debtor, it is nevertheless possible to argue that this is useful, and even necessary, in balancing the debtor's interests with those of other parties.

Further, when compared to the United States, the somewhat reduced scope of quick sales in Canada can be viewed in a positive light, allowing for greater oversight during the process. As noted, quick sales are becoming increasingly popular in Canada; however, at present, preplan asset sales remain more popular in the United States. The additional requirements placed on sales to persons related to the distressed company serve as another judicial check on the quick-sales process in Canada. Specifically, under the new section 36(4), if a proposed sale is to a person related to the company, the court may only grant authorization if satisfied that "good faith efforts were made to sell ... the assets to persons who are not related to the company; and the consideration to be received is superior to the consideration that would be received under any other offer made in accordance with the process leading to the proposed sale."[169]

Moreover, the extra requirement under the CCAA that debtors pay the superpriority charge for any arrears on wages and pensions persists during a quick sale. As such, while Canadian debtors can theoretically dispose of their assets freely during a preplan sale, in reality, the assets

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166 *Report of the Task Force on the CCAA to the Bankruptcy and Insolvency Advisory Committee Working Group on Commercial Reorganizations, Bankruptcies and Receiverships* (1994) at 3 [emphasis added], cited in Kent et al, *supra* note 39 at 14.

167 (1999), 12 CBR (4th) 144 (available on QL) (BCSC).

168 *Ibid* at para 20.

169 *CCAA*, *supra* note 3, ss 36(4)(a)-(b).

are never entirely "free and clear" of charges and obligations. Rather, with regard to employee claims, a quick sale under the CCAA cannot proceed unless the debtor meets the mandated requirements beforehand. Outlined in subsection 36(7) of the CCAA, these requirements are compliance with subsection 5(a) of the CCAA (as discussed above) and paragraph 6(4)(a) of the CCAA (which relates to default of remittance to the Crown). Although in larger American Chapter 11 cases employees are typically paid in full through "first day" orders, the US Bankruptcy Code at least provides the option to sell without paying employees—a policy decision that may represent a real cultural distinction between the two jurisdictions.[170]

Despite the benefits of the Canadian quick-sales regime—with its greater emphasis on oversight and the balancing of key interests—there are still situations in which the more established American framework is more efficient. For example, in the United States, a distressed corporation does not need to prove that it is insolvent prior to pursuing a preplan sale, as it does in Canada. Further, American quick sales are not subject to the oversight of the monitor, who plays a key role in the Canadian process. As such, American debtors are able to seek court approval of a sale more quickly. These differences are particularly important in situations where time is of the essence because the debtor will soon be unable to meet its operating expenses. As such, the American process is apt to be more efficient in such "emergency" situations.[171]

Conclusion

Preplan sales are becoming increasingly popular in both Canada and the United States, with high profile insolvencies, such as those of Lehman Brothers, GM, and Chrysler, ending in quick sales in recent years. Although the Canadian quick-sales process under the CCAA has been likened to the American regime under section 363 of Chapter 11, there are nevertheless key differences in the way both countries approach preplan sales.

Indeed, the CCAA lacks the detailed statutory framework included in the United States Bankruptcy Code. Although recent amendments to the CCAA provide somewhat more guidance as to factors that courts should

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[170] Under the US Bankruptcy Code, employees have a priority claim for up to $10,000 in back wages, indexed for inflation (currently $10,950): 11 USC § 507(a)(4) (2006). But this claim is a priority unsecured claim—meaning that it comes after the claims of secured creditors—and of fourth priority, putting it after the costs of administering the debtor's estate. *C.f.* 11 USC § 507(a)(2) (2006) (priority for administrative claims).

[171] There does, however, remain the problem of creditors manufacturing such emergencies.

weigh in considering whether or not to approve a preplan sale, they do not outline a specific process through which asset sales are supposed to occur.

The Canadian approach to preplan sales does, however, include a number of checks in order to ensure that the process is fair and efficient. Particularly, Canadian courts are required to appoint a monitor during all CCAA proceedings. While the monitor can certainly be viewed as an impediment to an efficient asset sale—as, in practice, the debtor must secure the monitor's approval prior to any sale—the monitor has the potential to play a critical role in balancing the interests of both the debtor and creditors.

In essence, the questions of speed and certainty mark the biggest difference between quick sales under the CCAA and Chapter 11. On the one hand, the US approach is more likely to facilitate quicker asset sales; this efficiency of the US framework is necessary in large cases where the complexity of the business and the extent of the distress warrant an expedient response. On the other hand, the Canadian quick-sales process under the CCAA—though potentially less efficient than the American regime—provides better protection for employee claims, and utilizes the monitor as an independent advisor in order to balance the needs of both the debtor and its creditors.

Ultimately, while there are undoubtedly benefits to both systems, during a more traditional reorganization, the checks and balances provided by the CCAA are beneficial, insofar as they prevent the overuse of quick sales and provide greater oversight for the sales process.