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Canadian Association of Insolvency and Restructuring Professionals
Association canadienne des professionnels de l'insolvabilité et de la réorganisation

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October 18, 2022

BY E-MAIL – FINA@parl.gc.ca

Standing Committee on Finance
c/o Peter Fonseca, M.P.
Chair of the Committee
House of Commons
Ottawa ON K1A 0A6

Re: FINA review of Bill C-228

Dear Mr. Fonseca:

We are writing to you in advance of your study on Bill C-228, *An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, and the Pension Benefits Standards Act, 1985* (the *Pension Protection Act*, or "PPA").

We have attached as an Appendix to this letter a short description of our organisation, the Canadian Association of Insolvency and Restructuring Professionals ("CAIRP"), for your reference.

We consider that the changes contemplated by the PPA are important issues that warrant careful consideration and analysis, and we have set out hereunder our thoughts on the likely impact of the provisions as drafted, from our perspective. We would very much appreciate an opportunity to meet with the members of the House of Commons Standing Committee on Finance ("FINA") to discuss the matters raised herein.

CAIRP's interest in the issue under review

You will note from the attached Appendix A that CAIRP's mission includes advocating for a fair, transparent, and effective insolvency and restructuring system throughout Canada.

The questions raised by the PPA touch on several aspects that are a close focus of the insolvency and restructuring system, namely:

1. The protection of a vulnerable class of persons, to assist these in having and maintaining an adequate standard of living so that they may avoid financial difficulties in their own personal affairs;

2. The fair and equitable allocation of limited resources amongst stakeholders; and

3. Promoting restructuring compromises and settlements rather than liquidation, to avoid the societal ills associated with a bankruptcy.

All three of the above aspects need to be considered at the same time, in an exercise of carefully balancing the interests of the various stakeholders, as sometimes an attempt at improving one of the elements will lead to a deterioration in the others, which can be detrimental to the insolvency system as a whole.

Bill C-228, which seeks to amend the *Bankruptcy and Insolvency Act* ("BIA")[1] and *the Companies' Creditors Arrangement Act* ("CCAA")[2], is not the first time that the issue of an enhanced protection for defined benefit pension plans has been considered and that a legislative fix has been suggested[3], and in fact it is not the only attempt in the current legislative session, since two other private member bills have been introduced which address substantially the same issue.[4] Our comments herein apply equally to the other bills that are before the House.

Protection of employees and former employees

The expectation of a pension benefit by an employee or former employee[5] is an important consideration in respect of the employment conditions, as it constitutes deferred compensation for services rendered. This entitlement warrants protection, firstly for reasons of fairness, and secondly to ensure that the employee can have an adequate standard of living after retirement, without fear of falling into financial difficulties or poverty.

The deferred compensation should be available, and when provided can and should be protected, but the important consideration is the way this is best achieved.

Bill C-228 suggests this should be achieved by creating a super-priority for the arrears in periodic payments (the "Special Payments") required to amortize the deficit of a defined benefit pension plan ("DB Plan") and for the actuarial deficit itself.

We believe this measure is likely to be ineffective, and in fact will likely lead to a deterioration in the benefits available to workers in general, for the following reasons:

1. The super-priority contemplated would come into effect when an employer is bankrupt, in receivership or undergoing a restructuring process, i.e. in cases where the employer is clearly insolvent. From experience, we know that the assets of insolvent businesses have a greatly diminished value in a liquidation in the context of a bankruptcy or receivership proceeding. The value is preserved when the enterprise can be maintained as a going concern.[6] As such, the "protection" granted through the super-priority would be illusory, as the assets are likely to be insufficient to cover the unfunded pension deficit and Special Payments arrears.

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1 *Bankruptcy and Insolvency Act*, RSC 1985, c. B-3, as amended ("BIA").

2 *Companies' Creditors Arrangement Act*, RSC 1985, c. C-36, as amended ("CCAA").

3 Written submissions were made by CAIRP in connection with the review of Bills C-476, C-487, C-501, S-214 and S-216 (40th Parliament, 3rd Session), in the context of the Statutory Review of the *Bankruptcy and Insolvency Act* and the Companies' Creditors Arrangement Act undertaken in 2014 by Industry Canada (now Innovation, Science and Economic Development Canada ("ISED")), and in the context of the consultation on enhancing the retirement security for Canadians undertaken in 2018 by ISED. These submissions can be provided on request.

4 Bill C-225 (44th Parliament, 1st session) presented by Mr. Blaikie and Bill C-264 (44th Parliament, 1st session) presented by Mrs. Gill.

5 For ease of drafting, employees and former employees, workers and retirees are collectively referred to herein as "employees".

6 See for example, Re Ted Leroy Trucking (Century Services) Ltd., 2010 SCC 60 at par. 12 and 15, and Canada v. Canada North Group Inc., 2021 SCC 30 at par. 20.

2. Even though the super-priority contemplated in Bill C-228 would only come into effect five years after the PPA comes into force, we consider it is likely that the provision contemplated will cause employers to discontinue their DB Plans and offer employees defined contribution pension plans ("DC Plans") in their stead, or will impede the creation of new DB Plans, due to pressure from the lenders' community that will perceive the provision as an added risk that may affect the security for their advances. The conversion of DB Plans into DC Plans, or the failure to set up new DB Plans will have a detrimental effect on employees in general, as it will likely lead to less retirement protection, or a transfer of the risk related to changes in market conditions from the employer to the employee.

3. Furthermore, we consider that a "super-priority" to ensure that unfunded pension liabilities are paid ahead of claims of secured creditors would carry a very high risk of hampering the access to credit, as the secured lenders would then have no way to monitor risk. The unfunded liability is an estimate made from a series of calculations that may take some time to perform and that will change with time based on temporary changes in the underlying value of investments. As such, the exposure of lenders to a "super priority" that cannot be known or predicted is likely to cause a contraction of the credit, due to a risk that is difficult to assess or manage.

   That contraction of credit could affect solvent companies' access to the credit markets and would therefore affect the economy as a whole. As well, this contraction of credit may have the perverse effects of triggering the insolvency of a business that could otherwise be solvent and/or restricting an insolvent business' access to interim financing during the restructuring process, which would be counterproductive to the objectives of insolvency legislation and would not be helpful to the goal of protecting retirement income of workers.

   We agree that a five-year delay to implement the measure may dampen the impact of the credit restriction referred to herein, however we consider it likely that some restriction may still occur, which would be detrimental to the economy and to workers in general.

Based on the above, we consider that other means of protecting the employees' deferred compensation may be more appropriate and should be investigated further. This would include, for example:

- Measures designed to better capitalize the DB Plans, to limit or avoid situations of actuarial deficits. We consider that improving the funding rules when the business is solvent, profitable and successful is a better way to secure the benefits of employees than relying on the existence or value of assets at the point of insolvency.

- Keeping with an objective of ensuring that the DB Plans are well funded and remain funded ahead of any financial difficulty, measures should be implemented to better monitor the financial health of the DB Plans.

- Measures could be implemented to establish an insurance fund to indemnify employees if a DB Plan is terminated when in a deficit position.

Rationale

The issue of protecting pension plan benefits is an important one. It is widely accepted that pension plans are part of employees' compensation for services rendered and constitute a deferred salary for work performed. Employees are a vulnerable group as they do not readily have means to secure the amount that they are owed by the employer by way of deferred salary, and they need these funds to ensure they

have a proper standard of living on and after retirement, to avoid falling in financial difficulties or poverty during the retirement years.

The last annual survey published by Healthcare of Ontario Pension Plan ("HOOPP")[7] mentions that Canadians are growing increasingly concerned about day to day cost of living increases, and the capacity to save is dissolving for working Canadians. Mindful of these concerns, two thirds (66%) of Canadians would rather have a lower salary and a pension (or a better pension) than a higher salary and no pension (or worse pension), and 75% (an increase of 7% since 2021) of Canadians agree there is an emerging retirement crisis, and there is widespread support (over 75%) for the proposition that there is a societal benefit to pensions. Based on the same survey, "finding a job with a defined benefit pension plan" is considered to be among the 4 most effective ways to save for retirement by respondents, and the most effective way among respondents aged under 35.

The concerns are understandable, in particular in view of the decrease in pension plans offered to employees in the Canadian workforce. The information reported by Statistics Canada suggests that from 1976 to 2021, the number of employees in the workforce (public and private sectors) grew from 9.7 million to 18.9 million, an increase of 93.5%, while the number of employees with a registered pension plan ("RPP"), whether a defined benefit plan ("DB Plan") or a defined contribution plan ("DC Plan") grew from 3.9 million to 6.6 million, an increase of 68.9%. During that period, the number of employees where the registered pension plan is a DB Plan increased by only 21.4%. The loss of coverage by DB Plans is all that more pronounced, when we consider that the number of employees in the public sector and education, which are largely covered by DB Plans, grew by 90.5% in the same period.

The decline in number of employees covered by a RPP (from 40.0% to 34.9% of the workforce) and employees covered by a RPP that is a DB Plan (from 37.4% to 23.5% of the workforce, including public sector and education) is illustrated in the table below: [8]

Year/Number (in thousands)	1976	1986	1996	2006	2016	2021
No of employees (total)	9,747.5	12,008.5	13,420.1	16,375.0	17,911.6	18,865.4
Employees with a RPP	3,902.5	4,668.4	5,149.9	5,690.6	6,261.8	6,593.3
Employees where RPP is a DB Plan	3,645.1	4,295.7	4,535.4	4,600.6	4,203.8	4,425.5
Public sector and education	1,321.5	1,535.9	1,719.6	1,982.2	2,171.2	2,517.6
Year/%	1976	1986	1996	2006	2016	2021
No of employees (total)	100.0	100.0	100.0	100.0	100.0	100.0
Employees with a RPP	40.0	38.9	38.4	34.8	35.0	34.9
Employees where RPP is a DB Plan	37.4	35.8	33.8	28.1	23.5	23.5
Public sector and education	13.6	12.8	12.8	12.1	12.1	13.3
DB Plans vs All RPPs	93.4	92.0	88.1	80.8	67.1	67.1

[7] Canadian Retirement Survey – April 2022 conducted for Healthcare of Ontario Pension Plan ("HOOP"), accessible at HOOPP - Canadian Retirement Study.

[8] Source – Statistics Canada, https://www150.statcan.gc.ca/t1/tbl1/en/cv.action?pid=1110009701#timeframe (Pension plan data) and https://www150.statcan.gc.ca/t1/tbl1/en/cv.action?pid=1410002301#timeframe (labour force characteristics).

The results of the survey published by HOOP and the information from Statistics Canada regarding the decrease in RPPs in general and DB Plans in particular, suggests that the problem of the availability of a pension plan for workers and retirees is as much a concern as the protection of amounts payable to employees when a plan does exist.

The implementation of measures to protect actuarial deficits in DB Plans is likely to affect the access to credit. We know this concern to be a serious one, because it has been raised by the lender community each time the measure has been contemplated in the past, and because we know that the lender community allocates credit facilities to borrowers and establishes prices for these credit facilities based on a number of risk factors that take into consideration (in particular, but not exclusively) profitability, predictable cash flows, industry characteristics, environmental, social and governance ("ESG") factors and available security.

The unfunded liability for a DB Plan is an estimate made from a series of calculations that may take some time to perform and will change with time based on temporary changes in the underlying value of investments and the characteristics of the workforce. As a result, the unfunded liability or actuarial deficit can change rapidly and significantly, which reduces the predictability of cash flows and profitability. As well, a super-priority to protect the actuarial deficit, will bring into question the availability of security to support advances.

All these factors will result in an increase in risk from the lenders, perspective, which will undoubtedly result in a chilling effect on the credit markets.

The likely reaction to this chilling effect would be that the lenders would exert pressure on their borrowers to reduce the perceived risk, and this can easily be accomplished by convincing employers to terminate DB Plans, or refrain from establishing new ones, and offer DC Plans instead.

This leads to the possibility of a decrease in the number of pension plans to provide retirement income security, and even if the number of plans remains the same, the most likely result will be a further reduction in DB Plans as compared to DC Plans. The impact of establishing a DC Plan instead of a DB Plan is in defining who, between the employer and the employee, suffers the risk of market disruptions. In a DB Plan, the employees' benefit is intended to remain constant notwithstanding the changes in market conditions, and the employer is responsible to compensate the changes in market conditions through higher (or lower) contributions over time. In a DC Plan, the employer makes a set contribution that is then invested by the employees and as such the employees have a loss or benefit based on the yield of the investments, when funds are drawn from the DC Plan.

A decrease in DB Plans as compared to DC Plans is not in the employees' advantage and is a likely collateral effect from the contemplated super-priority provisions.

Furthermore, the protection afforded by a super-priority is likely illusory, as the assets at the point of insolvency, when considered from a perspective of an outright liquidation and not as a going concern, are often of very limited value. This is evidenced by the statistics accumulated by the Office of the Superintendent of Bankruptcy ("OSB"), which indicate that 1,942 business became bankrupt in 2021, with declared assets of $530.8M and declared liabilities of $3,692.4M, i.e. a deficit on assets of $3,161.7M or

595.7%, and that for all files closed in 2021, dividends totalling $220.5M were paid in respect of liabilities totalling $11,071.2M, or a dividend rate of less than 2.0%.[9]

Keeping in mind the low expectations regarding the value of assets at the point of insolvency and the objective of promoting pension plans and if possible, DB Plans to address the need for retirement income security, we believe that measures that promote financial health of pension plans are preferable to a legislated super-priority. As such, we consider that funding rules and monitoring processes should be contemplated in order to avoid plan deficits. As well, acknowledging that problems can never be fully averted, we consider that the protection in the event of a plan termination after insolvency could be implemented through an indemnification scheme.

Fair and equitable allocation of resources

One of the principal tenets of insolvency legislation is the fair allocation of resources amongst similarly situated creditors, where a *pari passu* treatment is the rule, and a priority is the exception. The provisions contemplated by the PPA would create such an exception.

When dealing with a liquidation process in an insolvency context, the problem is one of allocation of scarce resources amongst stakeholders who are all meritorious. Unfortunately, there is no reasonable prospect of the resources being sufficient to satisfy all claimants, and that is evident from the statistics accumulated by the OSB, quoted earlier in this text.[9]

We do not suggest that a protection should be rejected out of hand just because it offends the *pari passu* principle that underlies insolvency legislation. All we are suggesting is that the decision to establish a protection through an exception should be carefully considered, as a protection afforded to one stakeholder group through the legislation will necessarily come to the detriment of other stakeholder groups, who consider themselves equally meritorious and who will lose any prospect of a recovery due to a multiplicity of super-priority charges.

Promoting restructuring, compromises and settlements

One of the objectives of insolvency legislation is to promote restructuring instead of liquidation, to preserve economic value of businesses.[10]

We are concerned that the super-priority contemplated by the PPA may adversely affect businesses' access to the restructuring provisions of the BIA and CCAA. We note that the provisions contemplated by the PPA would not require the immediate payment of the Special Payment arrears or pension deficit, but would require that the proposal or plan of arrangement contemplate that these amounts will be paid. Section 60(1.5)(b) of the BIA and section 6(6) (b) of the CCAA then provide that, as a precondition of approval of the proposal or plan of arrangement, the court must be satisfied that the employer can and will make the payments contemplated in the proposal or plan of arrangement, as the case may be.

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[9] Office of the Superintendent of Bankruptcy, report for 2021 accessible at Insolvency Statistics in Canada — 2021 - Office of the Superintendent of Bankruptcy Canada. The data quoted herein is extracted from Tables 3 and 10.

[10] Jean-Daniel Breton, "Concepts imported from the U.S – Something Borrowed or Something New? Imitation is the Sincerest Form of Flattery" in 2007 Annual Review of Insolvency Law, Janis P. Sarra ed., Thomson Carswell (Toronto). See also Re Ted Leroy Trucking (Century Services) Ltd., 2010 SCC 60 at par. 12 and 15-18, and Canada v. Canada North Group Inc., 2021 SCC 30 at par. 20.

As these amounts can be important, there is concern that, in the absence of an agreement that would trigger the exception referred to in section 65(1.6) of the BIA or section 6(7) of the CCAA[11], there is too much uncertainty as to the standard that will be applied by the Court to approve a proposal or a plan of arrangement, in light of the requirement in section 60(1.5)(b) of the BIA or section 6(6) (b) of the CCAA. Specifically, will the Court undertake a review of the business plan of the debtor to ascertain the likelihood that payments contemplated to be made in the future can and will be made? Or will the Court require the immediate payment of all such amounts in order to be satisfied that the condition is met? Or will some other standard be applied, that is yet unknown?

If the requirement becomes the immediate payment of all special payment arrears and of the actuarial pension deficit, then this would represent a harsher treatment for the pension liabilities than that available for other employers, as it would cause an acceleration of payments as compared to what is contemplated by the relevant pension legislation. Considering these payments can be significant, and considering that liquidity is often required in order to carry out the restructuring plan and return the operations to sustainability, this requirement may cause an otherwise viable enterprise to fail, thereby triggering the societal factors that are sought to be avoided by the restructuring objectives of the insolvency legislation, namely the loss of employment for the employees, the disruption in the supply chain for suppliers and customers, the loss of value of assets, and a general loss for the community.

Furthermore, the uncertainty associated with the application of the PPA and its effect if a restructuring is unsuccessful will likely have a detrimental impact on the ability to restructure businesses. The uncertainty arises more particularly from:

- A lack of clarity regarding the conditions to approve a proposal or a plan of arrangement;
- the changes that can occur in the market during the pendency of the restructuring process, which can trigger a pension deficit where none existed, or deepen the deficit;
- the lack of clarity regarding the ranking of the super-priority for the pension plan in the event the restructuring is unsuccessful and liquidation ensues.

These uncertainties are likely to adversely affect the availability of liquidity from interim financing, which can jeopardize the restructuring process.

We note that impeding restructuring activity is counterproductive to enhancing recovery prospects for employees whose DB Plan is in a deficit position. If the restructuring fails, this likely results in the termination of the plan, and as we have pointed out earlier in this letter, the results of a termination of the plan at the point of insolvency usually leads to a poor recovery. If the restructuring is successful however, the plan may be continued, in which case the plan's financial health may return in time, through the on-going contributions from the employer and changes in market conditions.

These situations are not typically well known, because there is a lot more publicity and noise around a financial failure than a successful restructuring, but examples of these situations would include Air Canada and Stelco.

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[11] Section 65(1.6) of the BIA and section 6(7) of the CCAA provide an exception, whereby the court needs not be satisfied that all of the amounts can and will be paid, if there is an agreement between the relevant parties that is approved by the relevant pension regulator.

Air Canada became insolvent and availed itself of the provisions of the CCAA in April 2003. At that time, its pension plans revealed a solvency deficit of $1.3 billion. In order to preserve cash, Air Canada obtained an authorization from the Court to suspend the Special Payments.[12] The restructuring occurred without there being a termination or amendment of pension plans. While some concessions were made to change the plans' provisions after the financial crisis of 2008-2009, these concessions were made consensually in the context of the negotiations of the collective bargaining between Air Canada and its employees. By May 2015, the plan was reportedly in a surplus position.[13]

Stelco filed an application for an initial order under the CCAA in January 2004, asserting that it was insolvent due to impending re-evaluation of its pension deficit, which would cause a cash liquidity in the foreseeable future. A contestation was made regarding whether the company was in fact insolvent, and thus whether the relief under the CCAA was warranted, but after a hearing the Court determined the company was insolvent. At that time, the pension deficit was estimated to be $1,252 million. The reorganisation proceedings followed course, with a plan of arrangement approved by the creditors in December 2005 and approved by the Court in January 2006. The resulting effect of the proceedings, from the employees' perspective, was that a new collective agreement was negotiated on beneficial terms, with an initial up-front payment of $400 million in the pension plans, and a payment plan over 10 years to pay the remainder of the solvency deficiency.[14]

Overall comments

To summarize, we are concerned that Bill C-228 may not achieve the objectives sought thereby, and may in fact have a detrimental impact on overall protection of employees' future retirement income and may limit restructuring opportunities, thereby frustrating the objectives of insolvency legislation and likely resulting in loss of employment for workers and loss of value for stakeholders in general. Specifically, we are concerned that:

- The super-priority contemplated by Bill C-228 will provide an illusion of protection without real benefit, due to the fact that assets at the point of insolvency customarily have little or no value;

- The super-priority provisions contemplated by Bill C-228 will likely cause a restriction in credit availability, the impact of which would be a gradual elimination of remaining DB Plans. This is likely to occur notwithstanding the five-year time frame to implement the super-priority, as the lender community is likely to manage the perceived risk by causing their borrowers to discontinue DB Plans. The foreseeable impact is a greater focus on DC Plans instead of DB Plans, and an acceleration of the existing progressive elimination of DB Plans.

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[12] Information obtained from the Initial Order made April 1, 2003 (paragraph 21) and the First Report of the Monitor dated April 17, 2003 (paragraph 51).

[13] Source: Information reported by Benefits Canada (https://www.benefitscanada.com/about-us-canadian-investment-review/), dated April 15, 2016, accessible at https://www.benefitscanada.com/news/bencan/how-air-canadas-pension-took-off-as-canada-posts-plan-sank-into-deficit/

[14] Aubrey Kaufman and Stuart Brotman, Developments and Trends in Stakeholder Rights: Labour as a Gatekeeper, 25 B.F.L.R. 93, 2009 (Carswell, Toronto). See also Re Stelco Inc., 2004 CarswellOnt 121 (Ont. S. C.) at para graphs 1 and 66. See also information reported by Benefits Canada, dated February 2017, accessible at https://www.benefitscanada.com/news/bencan/stelcos-long-battle-on-the-pension-precipice/

- The changes contemplated by Bill C-228 are likely to affect restructuring proceedings under the insolvency legislation, due to increased uncertainty, increased risk and decreased access to financing during the restructuring period. A decrease in restructuring activity in favor of liquidations would be to the detriment of stakeholders in general as it would lead to loss of employment and loss of value. Furthermore, successful restructuring proceedings in the past have resulted in an enhanced recovery for the DB Plans, as the actuarial deficits are not eliminated if the plan remains unaffected.

We consider that the objective of better protecting the deferred remuneration of employees is an important one that merits due consideration, analysis and implementation. However, we believe this objective should be implemented by other means that will be more effective and will not have an adverse impact on restructuring activity. We would be glad to participate in a process designed to develop solutions consistent with these principles.

Closing remarks

Thank you for your attention to this letter. As mentioned above, we would very much appreciate an opportunity to meet with the members of FINA to discuss this important issue.

Sincerely,

THE CANADIAN ASSOCIATION OF INSOLVENCY
AND RESTRUCTURING PROFESSIONALS

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Who we are

The Canadian Association of Insolvency and Restructuring Professionals / L'Association canadienne des professionnels de l'insolvabilité et de la réorganisation ("CAIRP") (www.cairp.ca) is Canada's national professional association of insolvency and restructuring professionals that represents approximately 950 general members and approximately 500 articling, life, corporate and honorary associates who also contribute to the breadth and unique expertise of CAIRP (collectively "Insolvency Professionals").

Over 90% of Licensed Insolvency Trustees ("LITs") licensed under Canada's *Bankruptcy and Insolvency Act* ("BIA"), are members of CAIRP. LITs act as trustees in bankruptcy, trustees under proposals, administrators of consumer proposals, receivers, all under the BIA, as well as financial advisers, monitors under the *Companies' Creditors Arrangement Act*, and other tum-around consultants. LITs have been involved in every major insolvency and restructuring filing in Canada.

CAIRP was founded in 1979 as a not-for-profit and non-partisan corporation designed to advance the practice of insolvency administration in Canada, as well as the public interest in connection with insolvency matters.

Mission

CAIRP advances the interests of its members and the public by:

- promoting excellence among members,
- providing relevant professional development,
- establishing and enforcing CAIRP's Rules of Professional Conduct and Standards of Professional Practice,
- maintaining rigorous certification standards and providing innovative education to aspiring insolvency and restructuring professionals, and
- advocating for a fair, transparent and effective insolvency and restructuring system throughout Canada.