

# LEGAL BRIEFS

## When businesses can't hang on...

BY JAN DEAN

Maybe it's all part of our Calvinist heritage, but there's a special stigma about individuals or companies that declare insolvency or bankruptcy. It seems to indicate a proclivity for reckless spending. Carelessness. Some moral defect. Some people may even suspect that the business is fine and that money to keep it afloat does exist – the top guy has it in a numbered Swiss account.

Douglas Hancock, founding partner of Daigle & Hancock LLP says there is a lot of 'terrible mythology' that paints bankruptcy as a scheme to defraud creditors. In fact, he says, "the implications of bankruptcy are devastating. Often the bankruptcy of a business leads to personal bankruptcies." Not to mention the domino-like effect when businesses go under and force dependent businesses, like suppliers, to fold as well.

The current economic situation, whether you call it a recession or a downturn, is putting many businesses in a position where they can't meet their financial obligations, or the value of the company's assets won't cover the obligations, or all the assets of the company are in the name of an insolvent person.

That's really the barebones definition of 'insolvency' according to the Bankruptcy and Insolvency Act.

A business that meets one of those definitions of insolvency can opt to declare bankruptcy, or try to work out a deal with its creditors through a Proposal. By filing a Notice of Intention to File a Proposal or making a Proposal to creditors, the insolvent company buys itself some breathing space to see if it is possible to negotiate a deal with creditors that reduces the debt load and enables it to continue in business.

A licensed trustee has to participate in the



Douglas Hancock, founding partner Daigle & Hancock LLP.  
Photo by Peter McCusker

process while creditors must first file their claims. Both creditors and the court have to approve the Proposal and it must offer a better option than bankruptcy.

If the proposal is not accepted, then the company moves into bankruptcy. Assets are liquidated and divided amongst creditors.

The Wage Earner Protection Act ensures that employee wage claims against employers who are bankrupt or in receivership get higher priority than even secured creditors, but there are limits. Where the employee is terminated by the process, he or she is limited to \$3,000.

If the insolvent company is fairly large and has debts of more than \$5 million, it can opt for the Companies' Creditors' Arrangement Act (CCAA) – a debtor-driven legal status that stays creditors and allows the company to put together a plan to decrease debt by negotiation.

Monitors appointed by the court oversee the process and report to the court on progress. The upside is giving the insolvent company time – the downside is the high expense of this process.

Under CCAA, the court can be flexible. The goal is to allow the insolvent company time to restructure itself and reduce its debts in ways that will allow it to continue as a viable business. This could mean selling the company as a going concern. If no remedies are found, the company and its assets are liquidated.

Robert van Kessel, a civil litigation lawyer with Lawrences of Brampton has made Insolvency and Bankruptcy (I&B) a focus for his practice. Van Kessel says Insolvency & Bankruptcy is a fascinating area of law – "there are always new issues, and it feels good to help people and businesses."

He says the regulations defining CCAA, which date back to the Great Depression of the 1930s, are "very skeletal". The process offers wide scope for developing a compromise plan and creditors – both secured and unsecured, share the pain.

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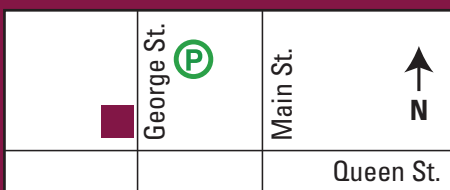
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# Fewer options for troubled firms

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Van Kessel says that the court no longer has the power to force changes – until recently the court could use its discretion to remake contracts. Going CCAA requires the appointment of a monitor who is the eyes and ears of the court, assembling information, reporting progress to the court and asking the court to approve the plan to survive, or the liquidation of the company. The court listens to all the parties involved and the monitor before adjudicating.

CCAA is a very expensive process but it does have advantages. If the court deems specific supplies essential, suppliers must continue to deliver to the CCAA company during the process.

CCAA was never intended to be a long process says van Kessel. "It was supposed to be expedient, to be concluded in a matter of months." That doesn't always happen and he cites Stelco as an example. The Hamilton-based steel giant was CCAA for 26 months because of the huge issues between management and the unionized workers. Stelco survived the CCAA process, but it still may not have a happy ending. The Canadian company was eventually sold to U.S. Steel. No one knows how 'temporary' the closure of its Hamilton Hilton works really is.

Van Kessel notes that many companies in trouble use the bills or taxes they haven't paid like an unauthorized line of credit – definitely not a good thing to do. But in industries like automotive, where a few giant companies have great power over myriad suppliers, a decision to delay payment ripples down. Initially the impact will be on their direct suppliers, but unpaid suppliers won't be able to pay their suppliers etc.

It comes as no surprise that business is picking up for lawyers who specialize in insolvency and bankruptcy. These are tough times – especially for manufacturing and nobody seems to have a handle on what is going to happen next.

Hancock says he would never have imagined the Prime Minister of Canada



**Bobby Sachdeva**

debating the economy with David Dodge, but then again nobody seems to be getting it right. "Jeff Rubin of CIBC predicted oil would hit \$200 a barrel and a few weeks later it was at \$30,"

Hancock says one difference he has noted in this recession is a reluctance to go to court. "In the last recession people seemed to sue each other; there was no sense of a rapid decline," he says. "Now in this recession, I see people and businesses trying to make a deal rather than go to court. They're hanging on to money."

Bobby Sachdeva, partner and head of Pallett Valo LLP's Insolvency & Corporate Restructuring Practice says that while businesses all over are feeling economic pain, the manufacturing sector is the first to go. The ranks of manufacturers have already been thinned out over the years thanks to the rise of the dollar and the move to offshore factories, but that process is speeding up, especially for auto parts manufacture.

Sachdeva says that when times get tough and money is scarce, investors become more risk-averse – less willing to put money into avant-garde businesses.

We hear about the big companies that go CCAA or end up declaring or being deemed



**John J. Ball**

bankrupt by the courts. What we don't hear much about are what Sachdeva calls the "quiet deaths and wind-downs" – all the smaller companies that simply close their doors, unable to continue doing business in this economic climate. Next time you see an empty parking lot in an industrial area or a sign offering a site for lease, you might wonder what happened to the business that used to inhabit that space. Did it move up to larger quarters? More likely in this economy, that it simply ended its existence "not with a bang but a whimper" (T.S. Eliot).

Sachdeva says simply that, "it's a different world. Two years ago insolvent businesses would have had a whole range of options available to them but times have changed," says Sachdeva. Credit is tight, and the 'short dip financing' that would have helped keep many businesses afloat simply isn't available. He cites Linens 'n' Things as an example, saying that three years ago the company would have likely found the refinancing it needed to survive.

For private companies, insolvency and bankruptcy can domino easily into personal bankruptcy. When John Doe's company runs into trouble, the bank might shorten the company's line of credit and demand a



**Robert van Kessel**

personal guarantee from the owner. If the business goes under John Doe will likely be wiped out.

There is a rhythm to I&B during recessions. John Ball, partner at Keyser Mason Ball LLP says he anticipates that his firm will be busy with struggling businesses this summer. "Generally a lot of this stuff happens behind the wave as companies try to hang on," explains Ball.

He says companies that end up bankrupt can get there in a variety of ways.

Sometimes the business owners simply say "I give up" and opt for bankruptcy. In other cases a creditor gets upset and asks the court to declare a company bankrupt. That can be high risk for the creditor – if the bankrupt company doesn't have cash or assets to cover the legal costs, the creditor is on the hook for those expenses.

For companies in trouble, Ball says it's much better to keep key creditors informed about the situation – that way you can co-operate with them and potentially cut a deal that will keep your business going. It's a tough process to go through and there's a lot of pain involved – "this time around, there's a lot of people you feel sorry for," says Ball.

## Developer will be ready when consumer confidence returns

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Of course, the most important part of the project is the introduction of 350 new residential units, including 12 loft units on the Mill Street facade, which will include two stories and a rooftop terrace or sunroom.

The design of the building, created by Sirlin Giller & Malek Architects in partnership with AREA Architects Ltd., will feature a nine storey podium with a 26 storey tower protruding from that. On top of the nine storey podium there will be an outdoor recreation area with patios and terraces. Meanwhile, the building will also have a lap pool, exercise room and meeting rooms for all of its residents, as well as two units that will be rented out to guests of condo owners like hotel suites. According to Robinson, the building will also be LEED certified with "extensive landscaping" in the front and a public art installation on Railroad Street.

While Preston Group has already started taking registrations for units on the website [www.leadcondos.com](http://www.leadcondos.com), the sales office isn't set to open until the fall of 2009. It will be located at the corner of Queen Street and Park Street once it's up and running. The purpose of the registration, explains Robinson, is to give potential buyers the first chance to land the unit of their choice. "When you have a grand opening, typically two days before you have an opportunity for the people who've registered to come in and be first in line," she says. There are currently almost 200 people registered, which Robinson says they're pleased with given the state of the economy.

"We obviously do hope that the economy will pick up in time for when we have our grand opening," says

Robinson. Fortunately, the economy will have some time to get in gear before selling really becomes an issue. Robinson estimates that it will take a year to build and, based on previous projects in downtown Brampton, a year or two to sell out. "We're not that concerned because with the economy down right now and people [not] buying, we're hoping there's pent-up demand when we do come on the market," says Robinson. Though, she does acknowledge that the pressure to sell does exist, as they will need to have sold probably three quarters of the units before they can even begin construction.

Besides the glitz and the glamour of commercial space, athletic facilities, terraces and beautiful design, Preston Group is banking on the building's proximity to the downtown GO Station to attract buyers. Construction is already underway to transform what is now a commuter service into a full service line. That means that instead of a mere four trains in the morning and four at night, there will be trains coming and going all day and all week, weekends included. Bridges and tracks will be widened between Brampton and Toronto in order to increase service. "Certainly by the time people move in, it'll be a full service line," says Robinson. That's a huge plus to anyone who commutes on a daily basis from Brampton to Toronto, or who would simply prefer to avoid driving.

The Blade Condo Project is currently waiting for site plan approval. Building will start just as soon as consumers are ready to take advantage of what living in a condominium in downtown Brampton will mean for them, their way of life and the city in years to come.

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