



The Subordination of Securities Law Claims in Insolvency Proceedings

Victor Barta
UBC Law
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I. Introduction

In an increasingly competitive global marketplace, where capital, information and ideas travel further and faster than ever before, investors have access to a myriad of traditional and modern, sophisticated financial instruments. At their core however, investments are of two basic types, debt and equity.

One of the basic distinctions between a debt and equity investment in an incorporated company is that shareholders, while not guaranteed any return on their investment, participate in the theoretically unlimited upside potential of the company, through dividends or capital gain. Lenders, on the other hand, receive a return on their capital based on the contract governing the debt, subject to the downside risk of losing their principal. In the event of the company being liquidated, shareholders rank behind creditors in the distribution of the company's assets and are therefore likely to lose some or all of their equity investment. This is the trade-off shareholders bargain for in exchange for an unlimited potential return.

With easier access to capital and markets, great successes abound, as do spectacular failures. Securities law and insolvency law serve to protect investors both in times of a company's growth as well as during its contraction and dissolution. Securities law is primarily focused on investor protection and the creation of efficient and transparent capital markets. Insolvency law serves to facilitate, where possible, the rehabilitation of financially distressed companies or, a fair and orderly liquidation of their assets. Both regimes serve important public policy functions. One such function, served by insolvency law, is the maintenance of efficient credit markets. This goal is achieved, in part, by providing certainty in the order of priority of claims against a company's assets. A creditors' priority, whether secured or not, over shareholder claims factors into the pricing of credit. Subordination of their claims is part of the ordinary business risk faced by equity investors.

In recent years, bankruptcies of an unprecedented scale, coupled with equally surprising fraudulent activities by management, raised the question of whether claims by equity investors occasioned by a company's breach of securities laws should rank *pari passu* to other creditor claims. The crux of the argument in support of elevating the status of these claims is that breach of disclosure laws, particularly to the degree witnessed recently, is outside the scope of risk for which shareholders bargain. Those opposed fear further damage to already unstable credit markets by introducing a new set of potential claimants, whose existence and resulting potential dilution of the company's assets was not contemplated in the original credit pricing decision.

Aside from engaging our notion of fairness, this intersection of securities and insolvency law raises the potential of uncertainty in the characterization of claims or worse conflict between the regimes.

II. Sarbanes-Oxley: Conflict in US Securities and Bankruptcy Laws

The Securities and Exchange Commission (“SEC”) is empowered by Congress and describes its mission as being: “to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.”¹ In that capacity, the SEC has statutory authority to conduct informal inquiries and formal investigations to ensure compliance with securities laws and its own regulations. Where a violation has occurred, the SEC may apply to a court for, or impose administratively, a wide range of remedies. Common remedies sought by the SEC include trading suspensions, disgorgement of illegal profits, and the imposition of civil penalties.² Historically, collecting damages for injured investors has not been a major focus of the SEC.³ Recovering money for investors' losses, instead, has been the function of private litigation, including securities fraud class actions. This changed dramatically in 2002.

In reaction to a series of corporate scandals including Enron and WorldCom, the United States Congress enacted the *Public Company Accounting Reform and Investor Protection Act of 2002*, better known as the *Sarbanes-Oxley Act of 2002* (“*Sarbanes-Oxley Act*”),⁴ which is chiefly designed to foster enhanced accountability on the part of corporate auditors, officers, and directors.⁵ Violations of the Sarbanes-Oxley Act are deemed a violation of the rules and regulations of *Securities Exchange Act of 1934*⁶ (“the *Exchange Act*”), subjecting wrongdoers to the same penalties assessed under that statute.⁷

An important element of the *Sarbanes-Oxley Act* is Section 308 (the “Fair Funds provision”). This provision gives the SEC a more prominent role in compensating defrauded investors. Prior to the enactment of the Fair Funds Provision, civil penalties were deposited into the U.S. Treasury. Pursuant to the Fair Funds Provision, however, the SEC may add civil penalties assessed in enforcement actions to funds obtained through disgorgement orders, and then distribute the entire pool of assets to investors who have been harmed by those violations. From 2002 through February 2010, \$9.5 billion in Fair Funds were ordered. Of that, \$9.1 billion (96%) has been collected and \$6.9 billion (76%) of the funds collected has been distributed.⁸

While it is unclear what percentage of these amounts relates to funds collected from insolvent corporations, s.308 has been applied in the case of judgments against insolvent companies that have filed for bankruptcy protection. Perhaps the most noteworthy of these cases was *SEC v. WorldCom Inc.*⁹

¹ <http://www.sec.gov/about/whatwedo.shtml>

² Wendy S. Walker et al., “At the Crossroads: The Intersection of the Federal Securities Law and the Bankruptcy Code” (2007) 63 Bus. Law. 125 at 127-128.

³ Barbara Black, “Should the SEC Be a Collection Agency for Defrauded Investors?” (2007) 63 Bus. Law. 317 at 318.

⁴ *Sarbanes-Oxley Act of 2002*, Pub. L. No. 107-204, 116 Stat. 745, codified in Titles 11, 15, 18, 28 and 29 U.S.C. (2002).

⁵ *Supra* note 2 at 126.

⁶ Securities and Exchange Act of 1934, sch. 404, Title I, 48 Stat. 881 (codified as amended at 15 U.S.C.A.) §§ 78a-78nn.

⁷ *Supra* note 2 at 131-132.

⁸ United States Government Accountability Office, “Securities and Exchange Commission: Information on Fair Fund Collections and Distributions” (2010) <http://www.gao.gov/new.items/d10448r.pdf>

⁹ 273 F. Supp. 2d 431 (S.D.N.Y. 2003), [*WorldCom*].

where, upon approval by the bankruptcy court of the plan of reorganization, defrauded shareholders became entitled to USD 500M in cash and USD 250M in stock of the reorganized company, the cash coming from WorldCom's bankruptcy estate.¹⁰ The court in *WorldCom* noted contentions by objectors to the settlement that distributing funds to defrauded shareholders via the Fair Funds provision violated the absolute priority rule in section 510(b) of the Bankruptcy Code¹¹ subordinating shareholder claims but the court refused to rule conclusively on this issue.¹²

The Fair Funds provision of the Sarbanes-Oxley Act does in fact circumvent a key tenet of the United States Bankruptcy Code. Chapter 11 of the Bankruptcy Code is designed to facilitate reorganizations by enabling a debtor to formulate a confirmable plan, specifying the proposed distributions to creditors and, where applicable, equity holders. A fundamental principle of Chapter 11 is the absolute priority rule which stipulates the priorities of creditors and provides that creditors of all types must be paid in full prior to any distribution to equity holders.¹³

The Fair Funds Provision of the Sarbanes-Oxley Act is directly at odds with a key principle underpinning US insolvency law. Courts in the US have recognized this tension¹⁴ and Congress should address it and ideally adopt reasoning similar to the Australian legislature in its decision to reverse the *Sons of Gwalia* decision.

III. Australia: Reversing the *Sons of Gwalia* Decision

Sons of Gwalia was Australia's third largest gold producer and controlled more than half the world's production of tantalum. After suffering hedging losses and falling gold reserves, the company collapsed with in excess of \$800M in debts. The complainant, Mr. Margaretic, claimed that the company acted in contravention of various corporate and securities laws¹⁵ and that he was a victim of misleading and deceptive conduct and therefore entitled to compensation. In the case of a solvent corporation, there would be nothing extraordinary about such a claim. Australian law, however, is clear that in the case of

¹⁰ For a more complete description of the sequence of events in *WorldCom*, see: Zack Christensen, "The Fair Funds For Investors Provision Of Sarbanes-Oxley: Is it Unfair to the Creditors of a Bankrupt Debtor?" (2005) 2005 U. Ill. L. Rev. 339 at 355.

¹¹ The Bankruptcy Code as amended is codified in Title 11 of the United States Code, 11 U.S.C.A. §§ 101-1532 [Bankruptcy Code].

¹² For a more complete description of the sequence of events in *WorldCom*, see: Zack Christensen, "The Fair Funds For Investors Provision Of Sarbanes-Oxley: Is it Unfair to the Creditors of a Bankrupt Debtor?" (2005) 2005 U. Ill. L. Rev. 339 at 357.

¹³ *Supra* note 2 at 127.

¹⁴ *Supra* note 2 at 127; *Supra* note 12 at 357.

¹⁵ Mr. Margaretic claimed that Sons of Gwalia had engaged in misleading and deceptive conduct and breached its disclosure obligations under: Section 52 of the *Trade Practices Act 1974* (Cth); Section 1041H of the *Corporations Act 2001*(Cth); and Section 12DA of the *Australian Securities and Investment Commission Act 2001* (Cth).

an insolvent corporation, shareholders (referred to as 'members' in Australia) are to have their debts repaid only after all other debts are satisfied.¹⁶

Mr. Margaretic argued that his claim should not be viewed through the lens of his position as a member. He argued that if money is paid to the company to *create* the relationship of member (as will be the case when a person subscribes for shares), the company's obligation to pay damages for fraudulent misrepresentation inducing that subscription, or to pay damages because loss was occasioned by the company's misleading or deceptive conduct, should not be viewed as an obligation consistent with the legislated rights and duties of members.

All three levels of the Australian court system accepted Mr. Margaretic's argument, with the High Court rejecting the appeal of the Company's administrators (akin to our liquidators or receivers) in a 6 to 1 decision. The majority, in separate judgments, rejected the suggestion that the *Corporations Act* embodies a general policy of "members come last"¹⁷ in corporate insolvency and concluded that the expression in section 563A "in the capacity as a member"¹⁸ suggested that shareholders may have claims in a capacity otherwise than as members. Section 563A therefore simply operated to subordinate claims by shareholders in their capacity as shareholders, such as a debt owed to a member by way of dividend.

The lone dissenting judge relied on statutory interpretation¹⁹, authority²⁰ and most importantly, policy²¹ in his support of the appellants. He articulated flood-gate type reasoning, envisioning scenarios where all the shareholders of an insolvent company could have similar claims that would be elevated to the status of unsecured creditors, thereby eroding creditors' rights to "less than a trickle".²² This sentiment was echoed by those who lobbied against the decision, arguing that it would result in more demands for security and higher interest rates to compensate for the increased risk, both of which could harm the financing efforts of corporate borrowers.²³

In addition to the risk creditors now faced of substantial dilution from shareholder claims in fraud situations and the risk of substantial delay in distributions while shareholder claims are adjudicated by the insolvency administrators, the decision also introduced the specter of shareholders with unproven

¹⁶ S. 563A of the *Corporations Act* in Australia, provides that: "Payment of a debt owed by a company to a person in the person's capacity as a member of the company, whether by way of dividends, profits or otherwise, is to be postponed until all debts owed to, or claims by, persons otherwise than as members of the company have been satisfied".

¹⁷ (2007), 232 ALR 232; [2007] HCA 1 at para. 19, [*Sons of Gwalia*].

¹⁸ *Supra* note 16.

¹⁹ *Supra* note 17, para's 227-229.

²⁰ *Ibid*, para's 243-250.

²¹ *Ibid*, para. 256.

²² *Ibid*.

²³ See for example: http://www.bracewellgiuliani.com/index.cfm/fa/news.advisory/item/fd24a284-197a-4994-b9dc-3ac618f3e501/The_Rights_of_Creditors_in_Australia_Restored_Sons_of_Gwalia_To_Be_Reversed_Through_Legislation.cfm

fraud claims holding sway over voting on whether to accept a restructuring package.²⁴ These combined to introduce a significant level of uncertainty into credit markets.

Perhaps this reasoning informed the Australian Minister for Financial Services, Superannuation and Corporate Law, who, in January 2010, released a package of reforms to Australia's corporate insolvency laws. The most significant of these reforms was an amendment to the *Corporations Act 2001* to reverse the effect of the High Court's decision in *Sons of Gwalia*. When brought into force, these amendments will bring Australian insolvency law back to where it was before the *Sons of Gwalia* decision with the addition of codification of the priority of unsecured creditors over all equity claimants, including those whose claims stem from allegedly fraudulent or misleading disclosure by the insolvent entity.

Reaction by both the legal community and securities and corporate governance professionals was overwhelmingly positive. The amendments are expected to have the effect of: returning certainty to external administration; encouraging debt investment in Australia; limiting some concern of banks at unsecured debt exposures and reducing lending costs; reducing insolvency administration costs; reducing class actions available to shareholders and litigation funders and restoring protection to debt markets ahead of equity markets.²⁵

Australian law's retreat from the controversial decision in *Sons of Gwalia* brings its laws back in line with those of Canada.

IV. Canada: Staying the Course

In Canada, insolvency proceedings are governed by the *Bankruptcy and Insolvency Act*²⁶ ("BIA") and the *Companies' Creditors Arrangement Act*²⁷ ("CCAA"), the latter being the primary tool for the reorganization or liquidation of larger insolvent entities.

²⁴ Because they had made a credible fraud argument and shown reliance on the misinformation in their share purchase decisions, the shareholders of Sons of Gwalia were allowed to vote the full amount of their (as yet unproven) claims on the proposed restructuring package. As a result, they had \$250M of the \$1.1B in claims that were eligible to vote. For more details see:

[http://www.bracewellgiuliani.com/index.cfm/fa/news.advisory/item/2108cb12-96f3-40bb-89d4-82407844ee46/Australia The Sins of the Sons of Gwalia Are Visited on Creditors Yet Again.cfm](http://www.bracewellgiuliani.com/index.cfm/fa/news.advisory/item/2108cb12-96f3-40bb-89d4-82407844ee46/Australia%20The%20Sins%20of%20the%20Sons%20of%20Gwalia%20Are%20Visited%20on%20Creditors%20Yet%20Again.cfm)

²⁵ National law firms Norton Rose, LAC and others published articles supporting the amendments as did the international law firm of Bracewell and Guiliani. See:

<http://www.nortonrose.com/knowledge/publications/2010/pub26015.aspx?page=100121040824&lang=en-gb> ;

<http://www.laclawyers.com.au/document/Reversal-Of-Effect-Of-Sons-Of-Gwalia-Decision--Ending-Of-Equal-Ranking-Of-Shareholder-Claims-With-Claims-Of-Unsecured-Creditors-In-Corporate-Insolvency.aspx> and

[http://www.bracewellgiuliani.com/index.cfm/fa/news.advisory/item/fd24a284-197a-4994-b9dc-3ac618f3e501/The Rights of Creditors in Australia Restored Sons of Gwalia To Be Reversed Through Legislation.cfm](http://www.bracewellgiuliani.com/index.cfm/fa/news.advisory/item/fd24a284-197a-4994-b9dc-3ac618f3e501/The%20Rights%20of%20Creditors%20in%20Australia%20Restored%20Sons%20of%20Gwalia%20To%20Be%20Reversed%20Through%20Legislation.cfm) The Chartered Secretaries of Australia, a national corporate governance organization, also released a letter in support of amendments. See:

http://www.csaust.com/AM/Template.cfm?Section=Australian_information&Template=/CM/ContentDisplay.cfm&ContentID=14339

²⁶ R.S.C. 1985, c. B-3.

A. The Common Law

The status of the common law, as it relates to equity claims in the insolvency context, was reviewed in *National Bank of Canada v. Merit Energy*.²⁸ The position of equity claims relative to debt claims is clear; they rank behind claims of creditors in insolvency. *Re Blue Range Resource Corp.*²⁹ was the first Canadian case to deal with the issue of whether equity investors, allegedly induced to purchase shares by fraudulently misleading information, could have their claims elevated to parity with unsecured creditors in a CCAA proceeding. The policy rationale that underlies the ranking of equity and debt claims in the insolvency context was identified by Romaine J. in *Blue Range* where she concluded that even defrauded shareholder claimants are presumed to have bargained for equity-type profits, and assumed equity-type risks, whereas creditors are presumed to have dealt with the company on the basis that their claims were in priority to such shareholder claims.³⁰

B. Characterization of Claims

Unsurprisingly, characterization of claims as being either equity or debt became a hotly contested issue and often presented the courts with a difficult interpretive exercise. The Supreme Court of Canada addressed the characterization issue in *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*.³¹ In that case, the court had to determine whether an agreement to participate in a portion of a bank's loan portfolio was an equity investment or a loan. The court noted that the characterization exercise was a matter of interpreting the agreements in question to see what the parties reasonably intended, and that the exercise could be a challenging one.³² In *CDIC*, the agreements included characteristics associated with both debt and equity financings, as do many modern hybrid financing instruments. The court concluded that, in substance, the agreement was a loan agreement. As reflected in the court's reasoning, reaching this conclusion was not a straightforward matter.³³

In *Re Central Capital Corporation*,³⁴ the Court of Appeal for Ontario had to characterize a claim arising from the right of retraction in respect of certain preference shares. The holders of those shares were asserting a claim under the *BIA* in respect of the right to require the company to redeem the preference shares. Although the relationship of the holders of the preference shares had characteristics of both debt and equity, the Court of Appeal held, in a split decision, that in substance, the holders of the preference shares had equity claims with respect to their right of retraction, which provides for the return of capital, not for the repayment of a loan.

²⁷ R.S.C. 1985, c. C-36.

²⁸ [2001] A.J. No. 918, 10 W.W.R. 305 [*Merit*].

²⁹ [2000] A.J. No. 14, 15 C.B.R. (4th) 169 [*Blue Range*].

³⁰ *Supra* note 29, para.33.

³¹ [1992] 3 S.C.R. 558, S.C.J. No. 96 [*CDIC*].

³² *Ibid.* at para. 51.

³³ See *Supra* note 31 at para. 54 where the court discusses the creativity of financial instruments and the difficulty of separating aspects that are central to the transaction from those which are merely incidental.

³⁴ [1996] O.J. No. 359, 27 O.R. (3d) 494 (C.A.) [*Central Capital*].

In a lengthy dissent, Finlayson, J.A. concluded that the retraction clauses in the appellant's shares created a debt with the meaning of the *BIA*.³⁵ Based on both plain language interpretation of the nature of a debt³⁶ and the substance of the contractual relationship³⁷, he concluded that "a fundamental error"³⁸ had been made in the characterization of the relationship. Based on the fact that the shares were not issued to the public in order to raise capital but were instead were issued to specific people for the purpose of acquiring specific assets, the shares, and their associated retraction rights, were in essence a loan, whose enforceability should not be subordinated by virtue of the holder's concurrent rights as shareholders.³⁹

C. Canada's Insolvency Law Reforms

The difficulties involved in characterizing claims and the associated divisions they created in the courts necessitated clarification from Parliament. The need for reform, and the suggested scope of the reform, was addressed in 2002 by the Insolvency Institute of Canada and the Canadian Association of Insolvency and Restructuring Professionals in the *Report of the Joint Task Force on Business Insolvency Reform*.⁴⁰ Using strong language in favour of subordination, the report addressed the kinds of claims that were at issue in *Central Capital*, *Merit Energy* and *Blue Range*. It recommended that amended legislation treat securities fraud and related claims as equity claims, subordinate to all other secured and unsecured claims.⁴¹ The Standing Senate Committee on Banking, Trade and Commerce came to the same conclusion in a 2003 report.⁴²

The amendments addressing the status of equity claims were presented in Bill C-12 in 2007,⁴³ and came into force on September 18, 2009 as amendments to the *CCAA* and *BIA*. The amended legislation clearly subordinates "equity claims" (defined very broadly), excluding that entire class of creditors from the right to vote on a plan or proposal unless the court orders otherwise and prohibiting the court from

³⁵ *Ibid.* at para. 32.

³⁶ *Ibid.* at para. 34-36.

³⁷ *Ibid.* at para. 37, 43-45.

³⁸ *Ibid.* at para. 37.

³⁹ *Ibid.* at para. 45.

⁴⁰ Insolvency Institute of Canada and the Canadian Association of Insolvency and Restructuring Professionals, *Report of the Joint Task Force on Business Insolvency Reform*, March 2002. For information on the background that preceded the amendments, see the excellent article by Janis Sarra, "From Subordination to Parity: An International Comparison of Equity Securities Law Claims in Insolvency Proceedings" (2007) 16 *Int. Insolv. Rev.* 181.

⁴¹ *Ibid.* Schedule A, Proposal 62.

⁴² Senate Standing Committee on Banking, Trade and Commerce, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act*, November 2003, at 158.

⁴³ Bill C-12, *An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005*. The legislation had a long history, having been introduced through a prior bill (Bill C-55) that was passed but never proclaimed into force. For the background, see: Legislative Summary, *Bill C-12: An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005*, accessed online at <http://www2.parl.gc.ca/Sites/LOP/LEGISINFO/index.asp?Language=E>

approving a plan or proposal that provides for the payment of an equity claim, unless all other claims are first paid in full.⁴⁴

Clarifying the subordination of equity claims was a key objective of the amendments. Industry Canada's clause-by-clause analysis of the amendments⁴⁵ notes, in reference to the provision in the CCAA restricting the voting rights of creditors with equity claims, that "[t]he amendment is one of several made with the intention of clarifying that equity claims are to be subordinate to other claims. Equity claims are ownership interests, and as such, should be subject to the risks of insolvency."⁴⁶

D. A Recent Review in *Earthfirst*

The recent case of *Earthfirst Canada Inc. (Re.)*⁴⁷ demonstrates how these amendments, had they been in force at the time of the decision, would have been determinative on the issue of characterization. Earthfirst was a developer of renewable wind energy whose capital structure included flow-through common shares. These securities have the features of common shares, but are supplemented by a feature that allows the issuer to transfer (or 'renounce') expenses related to project development activities to the holders of the securities. These expenses can then be applied against the earnings of the holder to reduce taxable income. If project development expenses are not renounced, the shareholder may lose part of the value of the original investment.

When Earthfirst issued its flow-through common shares, it agreed to incur and renounce certain project development expenses or, alternatively, to indemnify the shareholders in respect of the tax consequences of failing to do so. After commencing proceedings under the CCAA, a potential purchaser of Earthfirst's wind power project became concerned about not meeting the obligations under the flow-through shares agreement and incurring the associated expenses of indemnifying the holders. The Company therefore sought a declaration from the Court as to the nature of the holders' rights.

The case was decided by Romaine J., who wrote the *Blue Range* decision. Here, she had to consider whether the rights to indemnification that the holders of the flow-through common shares could have were debt claims or equity claims. Pointing to the difficulties faced by the Court in these borderline cases, she noted that "[t]his type of indemnity skirts close to the line that courts are attempting to draw with respect to the characterization and ranking of equity and equity-type investments in the insolvency context".⁴⁸

In deciding that the claims were in essence equity claims, Romaine J. considered the amendments to the CCAA that had been passed by Parliament but not proclaimed into force at the time.⁴⁹ While she could

⁴⁴ CCAA, ss. 2(1) "equity claim", 6(1), 6(8), 22.1; BIA, ss. 2 "equity interest", 54(2)(d), 54.1, 60(1.7).

⁴⁵ Industry Canada, *Bill C-12: Clause by Clause Analysis*, accessed online at: <http://www.ic.gc.ca/eic/site/bsf-osb.nsf/eng/br01978.html>

⁴⁶ *Ibid.* at <http://www.ic.gc.ca/eic/site/bsf-osb.nsf/eng/br01986.html#a78>

⁴⁷ [2009] A.J. No. 749, 56 C.B.R. (5th) 102 (A.B.Q.B.) [*Earthfirst*].

⁴⁸ *Ibid.* at para. 5.

⁴⁹ *Ibid.*

not apply these amendments to the claims of the holders of EarthFirst's flow-through common shares, the reference to them suggests that, had the amendments been in force, they would have been determinative of the issue. The amendments, if they could have been applied, would therefore have made the line-drawing exercise in the characterization of such claims much easier because the claims at issue are captured by the amended *CCAA*.

The amendments to the *CCAA*, and the related amendments to the *BIA*, were intended to have this effect. They make it easier to deal with equity claims in insolvency proceedings, and bring certainty to this area of the common law.

V. Conclusions

“[H]ealthy insolvency laws help to foster robust capital markets through certainty in credit decisions”.⁵⁰ The fragile nature of the world’s credit markets only serves to highlight the always present need for certainty in the order of creditor priorities. Even absent the market turmoil of recent years, shareholder claims resulting from securities law violations should be subordinated to the claims of other creditors. Numerous considerations inform this position including the public policy goals of fairness and certainty in securities and insolvency law as well as the efficient operation of credit and equity markets.

Hybrid financing instruments, that contain elements of both debt and equity, have posed the most challenging for Canadian courts to characterize in insolvency proceedings. Fortunately, our recently amended insolvency legislation draws a brighter line between the definitions of debt and equity investments. US law is not as internally harmonized, with the Fair Funds provision of the *Sarbanes-Oxley Act* providing shareholders with an end run around the absolute priority rule of the *Bankruptcy Code*. Hopefully the continued tension will likely cause in the American courts will result in an amendment to that legislation. All equity claims, including those arising from the violation of public statutes designed to protect investors, should come last in the hierarchy of claims in insolvency proceedings.

⁵⁰ Janis Sarra, "From Subordination to Parity: An International Comparison of Equity Securities Law Claims in Insolvency Proceedings" (2007) 16 *Int. Insolv. Rev.* 181 at 183.