A Disorienting Plunge from the Ivory Tower: Laurentian University and the Future of Insolvency Proceedings for Publicly Funded Corporations (PFCs) in Canada

A critical legal review of recent proposals to exclude publicly funded corporations from Canada’s insolvency regime

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April 2023
2805 Words
Introduction

The recently concluded *Companies’ Creditors Arrangement Act* (CCAA) restructuring of Ontario’s Laurentian University (LU) is forcing policymakers to evaluate the appropriateness of public institutions restructuring under an insolvency regime that was intended to be a remedy of last resort for corporations engaged in commercial activities. This is evidenced by three federal legislative proposals to exclude public institutions from the CCAA and the *Bankruptcy and Insolvency Act* (BIA), as well as further policy commitments from the Ontario Government to install greater oversight mechanisms over the governance and fiscal management of public institutions.\(^1\) The collective polity seemingly believed that governments would come to the aid of cash-strapped public institutions, and that the institutions would be glad to receive the help. Laurentian’s detour around Queen’s Park and onto the Commercial List, without first exhausting its recourse from the public treasury, has cast doubt over that intuitive assumption.\(^2\) The University restructuring has given rise to the question of whether CCAA restructuring is an appropriate tool for public institutions like universities, hospitals, and even municipalities. At least some federal legislators are unconvinced. Three pieces of legislation introduced in Canada’s federal Parliament have proposed to limit the ability of public institutions to seek relief under the CCAA as well as under the *Bankruptcy and Insolvency Act*. However, it is likely that these proposals will be ineffective if passed into law. Instead, this paper suggests that Canada ought to consider importing the state-consent feature of the U.S. chapter 9 regime.

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Laurentian University’s CCAA Proceedings

On February 1 2021, LU’s application for an initial stay of proceedings was accepted by Chief Justice Morawetz. Ernst & Young was appointed Monitor and Justice Sean Dunphy was appointed as Mediator to oversee negotiations regarding faculty contracts and the future of academic programming. In the initial phase of restructuring, LU downsized its programing and staff, terminating 158 faculty and non-faculty positions and cancelling 70 programs. The second phase focused on liquidating real estate assets under the supervision of a court-appointed advisor. Creditors approved a final plan of arrangement in October 2022, and by the end of November 2022 the University had satisfied all of the conditions of the implementation plan. The success of LU’s CCAA process is evidenced by the fact that a previously distressed university is continuing to provide post-secondary education for students. However, the restructuring significantly reduced academic offerings at the university and diluted access to bilingual post-secondary education in Northern Ontario. The significant redundancies, the scaling down of program offerings, and the pension plan adjustments have taken a further toll on the people of Sudbury.

The Government’s Response

Many seemingly believed that insolvency statutes would never be relied upon by public universities. This collective wisdom rested on the presumption that governments, as a vested

3 Laurentian University of Sudbury (Re), 2021 ONSC 659 [Laurentian].
4 Ibid. (Factum of the Applicant at paras 79-84); (Initial Order at paras 23-26).
6 Laurentian, supra note 3 (Seventeenth Report of the Monitor at paras 6-21).
7 Laurentian University of Sudbury, 2022 ONSC 5645 [Endorsement].
8 Torrie, supra note 5 at 6-8.
stakeholder and as a proxy for the public interest, would backstop struggling institutions with some combination of emergency financing and administrative supplantation.\textsuperscript{10} The LU insolvency proceedings turned this presumption on its head. Prior to and during LU’s \textit{CCA A} proceedings the Ministry of Colleges and Universities did not meaningfully intervene to correct Laurentian’s financial situation.\textsuperscript{11}

A January 25, 2021 letter from then Laurentian University president, Robert Haché, to the then Minister of Colleges and Universities, Ross Romano, requested $100 million in emergency liquidity to prevent the university's imminent filing under the \textit{CCA A}. This letter followed years of obfuscation on the part of LU, wherein the Board refused to share the university’s unvarnished finances with the ministry or work collaboratively with the government to bring the school into a sustainable fiscal position.\textsuperscript{12} It seems that LU further withheld from the Ministry that external counsel had been hired in early 2020 to start laying the groundwork for \textit{CCA A} protection.\textsuperscript{13} The Ministry responded to LU’s $100 million ask with an offer of approximately $12 million, citing an inability to meet the $100 million ask. This offer was contingent on LU not commencing \textit{CCA A} proceedings and agreeing to implement the recommendations of a ministry-appointed Special Advisor.\textsuperscript{14} Laurentian was not interested. A week later the university had filed and been granted its initial stay by Justice Morawetz.\textsuperscript{15}

\textbf{Interpreting the Law Regarding Publicly Funded Corporations and Insolvency}

LU argued in its initial application that the \textit{CCA A} applied to the university as a corporation incorporated through an act of the provincial parliament.\textsuperscript{16} Justice Morawetz agreed

\begin{itemize}
\item \textsuperscript{10} Sarra Janis, \textit{Creditor Rights and the Public Interest: Restructuring Insolvent Corporations}, (University of Toronto Press: 2003) at 15-18 [Janis].
\item \textsuperscript{11} AG Report, supra note 2 at 5.
\item \textsuperscript{12} AG Report, supra note 2 at 55-58.
\item \textsuperscript{13} Ibid at 59.
\item \textsuperscript{14} (Confidential Exhibit “EEE” Letter from the Ministry of Colleges and Universities to Laurentian University of Sudbury dated January 21, 2021).
\item \textsuperscript{15} Laurentian, supra note 3 .
\item \textsuperscript{16} Ibid (Applicant Factum at paras 27-52).
\end{itemize}
that the university’s structure did not exclude it from the CCAA’s definition of company. The court did not explicitly reference the unprecedented nature of a publicly funded university seeking out CCAA protection in its granting of the initial order. The absence of discussion or consideration afforded to the university’s public nature indicates the lack of apprehension the Commercial List had in ensnaring such an entity into the CCAA’s sphere. On its face, this seems consistent with the remedial purpose of the statute. As articulated in Re Metcalfe and Mansfield, the CCAA is “designed to be a flexible instrument and it is that very flexibility which gives the Act its efficacy.” Bankruptcy courts have inherent jurisdiction to do justice. Courts may exercise this jurisdiction when the insolvency statute is silent on the issue and the granting of the relief outweighs the relative prejudice to those affected by it.

Both the CCAA and BIA are silent on the eligibility of publicly funded institutions to initiate restructuring proceedings. The CCAA provides a broad definition of ‘debtor company’ which captures any company that is insolvent and has more than $5 million in debt. In Stelco the Ontario Superior Court affirmed a broader test for insolvency which held that a debtor is insolvent for the purposes of the Act if they were not yet insolvent but would become insolvent before a restructuring could reasonably be completed. A company is defined as “any company, corporation or legal person incorporated by or under an Act of Parliament or of the legislature of a province, any incorporated company having assets or doing business in Canada, wherever incorporated, and any income trust.” The act specifically excludes banks, telegraph companies,

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17 Laurentian, supra note 3 at para 29.
18 Metcalfe & Mansfield Alternative Investments II Corp., (Re), 2008 ONCA 587 at para 44 [Metcalfe].
19 See for example, Canada (Minister of Indian Affairs and Northern Development) v Curragh Inc. 1994 OJ No 953, 114 DLR (4th).
20 Residential Warranty Co of Canada Inc (Re), 2006 ABQB 236 at 26.
21 Companies’ Creditors Arrangement Act, RSC 1985, c C-36 [CCAA]; Bankruptcy and Insolvency Act, RSC 1985, c. B-3 [BIA].
22 CCAA, supra note 21 at s3(1).
23 Stelco Inc., Re, 2004 ONSC 24933 [Stelco].
24 CCAA, supra note 21 at 2(1).
insurance companies and companies to which the *Trust and Loan Companies Act* applies.\(^{25}\) The *BIA*’s definition of ‘corporation’ is virtually identical to the *CCAA*’s definition of company.\(^{26}\) In 1997, the *BIA*’s definition of ‘corporation’ was amended to remove the requirement that the entity have been incorporated for the purpose of ‘carrying on business’.\(^{27}\)

Canadian jurisprudence on Publicly Funded Corporations (PFCs) entering into insolvency proceedings is dearth and is largely confined to municipal insolvencies during the Great Depression.\(^{28}\) During the 1930’s, provinces intervened to amalgamate or restructure financially distressed municipalities. *Ladore v. Bennett* considered the provincially-mandated amalgamation of insolvent municipalities constituting modern-day Windsor. Creditors of the cities sought to have the amalgamation struck as *ultra vires*. They alleged that the legislated amalgamation was designed to cure matters pertaining to bankruptcy and insolvency, which are matters of federal jurisdiction. The Judicial Committee of the Privy Council (JCPC) affirmed that provinces are responsible for the welfare of municipalities, and that Ontario did not exceed the scope of its legislative jurisdiction in amalgamating the distressed corporations (municipalities).\(^{29}\) From the *Ladore* decision there exists common law authority for provinces to step in and restructure the affairs of an insolvent municipality or other incorporated entities under its control.\(^{30}\) This ambiguity between a right to intervene with a distressed municipality and a positive obligation to do so is further muddied by modern provincial statutes.\(^{31}\) For example, Ontario and several other provinces have amended their legislation respecting municipalities to allow for distressed municipalities to be placed under the control of provincially-managed


\(^{26}\) *BIA, supra* note 21 at 2(1).


\(^{28}\) *Municipal Insolvency in Canada, supra* note 27 at 1.


\(^{30}\) *Ibid* at para 5.

\(^{31}\) *Municipal Act, 2001 SO, c. 25, Part V [Municipal Act].*
boards. A similar provision exists for school boards and public hospitals. Unlike with universities, the provincial government has established a mechanism to appoint a supervisor to take over the board and administration of a hospital or school board. This is not a supplantation power reserved exclusively for instances of institutional insolvency, but is rather a Ministerial power of general application.

Where Statute Prohibits a PFC from Accessing Insolvency Remedies

Certain federal and provincial statutes prohibit certain PFCs from accessing the BIA or CCAA. For example, the federal statutes creating the Canada Mortgage and Housing Corporation and Canada Post contain such provisions. Ontario’s Municipal Act expressly states that municipalities cannot “become a bankrupt” under the BIA or make an assignment or proposal under that act (BIA) [emphasis added]. This paper has not canvassed the entirety of statutes enacting various PFCs, but it is clear that some provincial and federal statutes have sought to limit the availability of one or both of the insolvency regimes to certain public corporations. However, in considering the Quebec court’s decision in the 2013 Montréal, Maine & Atlantique Canada Co insolvency, these clauses may be of no effect. Here the court held that the CCAA’s explicit exclusion of railway companies was a nullity in the absence of alternative insolvency or restructuring legislation. The exclusion of railway companies from both the BIA and CCAA, with no legislated alternative for creditors to realize their rights, created an impermissible legislative vacuum. The court invoked principles of equity to allow for proceedings under the CCAA. The CCAA and BIA were subsequently amended to remove the exclusion of railway

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32 Ibid.
33 Not-for-Profit Corporations Act, 2010 SO 2010, c. 15.
34 Education Act, RSO 1990 c E.2, s 130.5; Public Hospitals Act, RSO 1990 c P.40, s 8–9.
35 Canada Mortgage and Housing Corporation Act, RSC 1985 c C-7, s 32; Canada Post Corporation Act, RSC 1985 c C-10, s 25.
36 Municipal Act, supra note 31 at s 17(g).
37 Montréal, Maine & Atlantique Canada Co. (Arrangement relatif à), 2013 QCCS 4039 [Montréal, Maine & Atlantique]
38 Ibid. at para 26.
39 Torrie, supra note 14 at 9
companies. This decision suggests that the legislated exclusion from both federal insolvency statutes, without the provision of a validly-enacted alternative regime, will be a nullity.

**Proposed Statutory Reforms**

There remains heightened concern about other public institutions with financial difficulties falling into insolvency proceedings. This is evidenced by the recent introduction of three pieces of legislation in Parliament. Bill C-288 and Bill C-309 (introduced in the House of Commons) and Bill S-215 (introduced in the Senate) all propose exempting PFCs from the BIA and CCAA. However, these proposals fail to offer an alternative for public corporations to remedy their insolvencies in the absence of the BIA and CCAA. If one accepts that a public corporation’s finances are not limitless (which there aren’t), and if creditors continue to lend to these institutions on their merits (which they seemingly will), then the fact of PFC insolvencies becomes a real possibility that law must contend with. Thus the choice for legislators is either to accept that public corporations are eligible under the BIA and CCAA (as Justice Morawetz did in the instance of LU), or to provide for a legally-sound alternative insolvency regime specific to publicly funded corporations. Excluding publicly funded corporations from the BIA and CCAA while failing to set out an alternative regime poses what Justice Castonguay referred to as “the risk of legal chaos” in the *Montréal, Maine & Atlantique Canada Co* insolvency.

The United States has dealt with this issue through chapter 9 of the *United States Bankruptcy Code*. During the Great Depression, the US Congress created a municipal bankruptcy regime to help local governments restructure their finances and avoid defaults caused by falling tax revenue and financial mismanagement. Chapter 9 developed a parallel but

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40 CCAA, supra note 21 s 2(1); BIA, supra note 21 s 2.
41 Supra, note 1.
42 *Montréal, Maine & Atlantique Canada Co*, supra note 37 at para 18.
43 11 U.S.C. sec. 109(c)
distinct insolvency regime for municipalities, who can only file under this chapter of the
*Bankruptcy Code*. This regime allows municipalities to benefit from the usual protections of an
insolvency restructuring while prohibiting the liquidation of a municipal debtor’s assets.\textsuperscript{45}
Insolvency restructurings of “municipalities” have been a more common phenomenon in the U.S.
than in Canada. Since chapter 9’s enactment in the 1930s, over six hundred public incorporated
entities (municipalities) have sought to restructure under its provisions.\textsuperscript{46}

The relevant features of chapter 9 are the prerequisite for the state to consent prior to the
municipality being able to commence an insolvency restructuring under the Code, as well as the
prohibition on the liquidation remedies of commercial bankruptcy.\textsuperscript{47} In order to commence a
restructuring under chapter 9 there must be clear and express written authority from the state.
The authority must be “exact, plain, and direct with well-defined limits so that nothing is left to
inference or implication.”\textsuperscript{48} There are additional distinguishing features of chapter 9 proceedings
from regular restructuring proceedings that are beyond the scope of this paper, such as the
enhanced ability for the municipality to effect changes with respect to collective bargaining
agreements.\textsuperscript{49} The legislation defines “municipality” as any “political subdivision or public
agency or instrumentality of a State.”\textsuperscript{50} Thus, the provisions ensnare a larger selection of
corporations than just municipal governments.\textsuperscript{51} In determining whether a corporation meets the
definition of municipality, American courts have considered whether the entity can raise tax
revenue, whether it exercises the power of eminent domain, and whether it is an instrument of

\textsuperscript{45} *Ibid* at 58.
\textsuperscript{46} *Ibid* at 46.
\textsuperscript{47} Veronica Lara, "Special Purpose Municipal Entities and Bankruptcy: The Case of Public Colleges" (2019) 36 Emory Bankr
Dev J 341 at 357-359 [Lara].
\textsuperscript{48} Trotter, *supra* note 44 at 48.
\textsuperscript{49} Clayton P. Gillette, "Fiscal Federalism, Political Will, and Strategic Use of Municipal Bankruptcy" (2012) 79 U Chi. Rev 281
at 289 [*Fiscal Federalism*].
\textsuperscript{50} United States Bankruptcy Code, 11 U.S.C. § 109(c).
\textsuperscript{51} *Re County of Orange*, 183 B.R. 594 (Bankr. C.D. Cal. 1995) at 604.
the state or public policy.\textsuperscript{52} The last factor is perhaps most relevant in the Canadian context. For instance, in a 2012 case concerning a publicly-funded hospital, the United States Bankruptcy Court for the District of South Carolina affirmed that the hospital was a municipality for the purposes of the Bankruptcy Code insofar as it was an “instrumentality of the state.”\textsuperscript{53}

The federalism considerations underpinning chapter 9 are particularly salient in the Canadian context of provincial and federal heads of power.\textsuperscript{54} Providing a federal mechanism for the restructuring of public entities, which are creatures of the various U.S. states, presented jurisdictional hurdles for Congress.\textsuperscript{55} The modern statute’s constitutional compliance is rooted in its necessitating local state consent for an entity under a state head of power to make an application to the federal bankruptcy court.\textsuperscript{56} By limiting the remedies available to municipalities under chapter 9, the regime is careful to ensure the entity that emerges from restructuring is materially the same entity. Where private debtors in bankruptcy will often emerge with different organizational structures, chapter 9 is limited to ensure that a municipal debtor emerges with new debt obligations but with the same organizational form.\textsuperscript{57} This reflects the public interest purpose of municipalities as a policy consideration.

**Discussion**

The LU case study shows that CCAA can be effective for distressed public institutions, but it is important to consider whose interests may be prejudiced in the process. Namely, the taxpayers who involuntarily fund the corporation through significant government grants and


\textsuperscript{53} In re Barnwell County Hospital, 471 B.R. 849 (Bankr DSC 2012).


\textsuperscript{55} In 1936, the U.S. Supreme Court found the original Municipal Bankruptcy Act to be unconstitutional for intruding on the state’s rights with respect to municipalities. See Trotter, supra note 44 at 53.

\textsuperscript{56} Anna Gelpen, "Bankruptcy, Backwards: The Problem of Quasi-Sovereign Debt" (2012) 121 Yale LJ 888 at 924.

\textsuperscript{57} Laura N. Coordes, “Restructuring Municipal Bankruptcy”, 2016 Utah L Rev 307 at 348 [Restructuring Municipal Bankruptcy].
allocations, and who in turn expect the provision of certain services in the public interest. The court has held that insolvency proceedings “involve a balancing of prejudices inasmuch as everyone is adversely affected in some fashion.” However, this has usually been applied to ensnare commercial parties who have consented to doing business with a party who subsequently becomes insolvent. The same agency (or privity) is not applicable to taxpayers when speaking of publicly funded institutions. The CCAA restructuring is not well able to attune for the broader public interests and is more squarely focused on the interests of creditors. Justice Côté articulated the public benefits of CCAA restructuring in Canada North, but also made clear that delivering the greatest net-benefit to the public is not the court's objective.

When considering whether CCAA or BIA restructurings are appropriate for PFCs, it is important to consider that these institutions are inherently political. Whether it be a university, hospital, or local school board—these incorporated entities are established to serve a particular public interest that is not inherently commercial. They are rightly influenced by the political cleavages of stakeholder groups and the public that they serve. That is not to say that regular commercial insolvencies are ignorant to public interest considerations. Century Services provides strong authority for the assertion that corporate restructurings often serve the public interest by allowing the business to continue as a going concern, sparing the employment, social, and economic fallout that would ensue in the event of the business’ closure or liquidation. However, existing scholarship suggests that insolvency restructurings are poorly designed to account for the non-economic political cleavages concerning PFCs. A business’ ability to implement top-down management changes in the best interest of the company’s emergence from insolvency

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58 Torrie, supra note 14 at 12
59 Metcalf, supra note 18 at para 117.
60 Canada v Canada North Group Inc. 2021 SCR 30 at para. 20 [Canada North].
is not analogous to a public institution's ability to implement changes that fly in the face of vested interest groups.

It is proposed that Canada consider the import of the *state consent* feature of the U.S. chapter 9 regime. Such a change would require the appropriate level of government to expressly consent to a publicly-funded corporation’s request to commence restructuring proceedings under the *CCAA* or *BLA*. This would vest the responsibility for the unique political considerations of insolvent publicly funded entities with democratically elected governments, which is their appropriate arena. The adoption of such a requirement would also guard against the particular facts of the LU insolvency: wherein a publicly funded corporation initiated *CCAA* proceedings without the government having a fulsome understanding of the university’s fiscal health.\(^{64}\) The Laurentian Board of governors had seemingly set their sights on *CCAA* as their preferred resolution without earnestly seeking out government support, essentially foiling any Ministry attempts to deter the proceedings.\(^{65}\) This reform would disallow such underhandedness. It would impose on governments an obligation to intervene with distressed publicly funded corporations where the facts warrant such intervention. Where government’s fail to intervene and permit the entity to enter insolvency proceedings, the public will have their say on such wisdom at the ballot box.

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\(^{64}\) *AG Report, supra* note 2 at 45.
\(^{65}\) *Ibid* at 8-9.