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THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE / COMITÉ PERMANENT DES BANQUES ET DU COMMERCE

EVIDENCE / TÉMOIGNAGES

OTTAWA, Wednesday, June 4, 2003

The Standing Senate Committee on Banking, Trade and Commerce met this day at 4:00 p.m. to examine on the administration and operation of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act.

Senator E. Leo Kolber (*Chairman*) in the Chair.

The Chairman: Good afternoon, ladies and gentlemen. The banking trade and commerce committee is meeting today to continue its examination of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act. Our first witnesses are from the Canadian Bar Association.

Welcome. It is a pleasure to have you. I understand that two of your members will be making opening statements. Please proceed.

Senator Kelleher: Honourable senators, before we start, I would like it noted for the record that two of the gentlemen appearing before us today from the Canadian Bar Association are partners of mine.

The Chairman: Well, we could give them our sympathies.

Senator Kelleher: I think they are aware of that.

The Chairman: This is a fact-finding thing and you have no conflict of interest.

Senator Kelleher: I know that. There will be no charge.

Ms. Tamra L. Thomson, Director, Legislation and Law Reform, Canadian Bar Association: Honourable senators, the Canadian Bar Association is very pleased to have the opportunity to appear before the Banking Committee today to make its comments on the five-year review of the Bankruptcy and Insolvency Act and the CCAA.

The Canadian Bar Association is a national association, which represents over 38,000 jurists across Canada. Among our primary objectives are improvements in the law and improvement in the administration of justice. With that point of view, we have made the written submission, which you have received and with which we make our oral statements today.

The introductory comments will be relatively brief. I will ask Mr. Cohen to address the corporate insolvency and reorganization issues with the assistance of Mr. Shea. Mr. Klotz will address the personal bankruptcy and insolvency issues, and then we will be pleased to take questions.

Before passing the floor to Mr. Cohen, I would like to say that the bankruptcy and insolvency law section of the Canadian Bar Association has long taken an interest in the issues related to

bankruptcy and insolvency reform. This is not the first exercise in reform where we have appeared before this committee. The comments build on those past submissions and, indeed, have been the result of consultations with section members across the country.

I will now ask Mr. Cohen to address the commercial insolvency issues.

Mr. David F. W. Cohen, Chair, National Bankruptcy and Insolvency Law Section, Canadian Bar Association: Thank you senators for having us here today. I will first address the corporate insolvency and reorganization submissions for the Canadian Bar Association. It is important, as a preface to our submissions, to note that the Canadian Bar Association's goals in making these submissions are, broadly speaking, focussed primarily on four issues. Those are accessibility of the legislation, fairness, efficiency and certainty.

Reference to these four touchstones of accessibility, fairness, efficiency and certainty in reviewing the Canadian federal liquidation and reorganization regimes is critical to formulating amendments and revisions to those regimes that enhance the utility and functionality of our system, both domestically and abroad.

(1610 follows, Mr. Cohen continuing: Our written submissions) IM June 4, 2003

(1600 precedes, Mr. Cohen: both domestically and abroad.)

(1610, Mr. Cohen continuing)

Our written submissions on the corporate matters today will deal with five points, which are submitted to you in writing. We will not deal with them all in our introduction. The first are priority issues, which give way to issues of fairness. The second is the participation, or what we call governance issues, which give rise to issues of accessibility and fairness issues competing with the issues of efficiency. The third is cross-border insolvency, which gives rise to accessibility and certainty issues; debtor-in-possession financing, which focuses on issues of efficiency and certainty, and interim receivership, which gives rise to issues of accessibility driven by uncertainty and fairness.

I would like to give an example of how we have used these touchstones in examining this legislation and the amendment of the legislation. As an example of the importance of the touchstones, we would like to briefly review our anecdotal experience in Canada and cross-border lending and insolvency matters. American participants in large reorganization cases, which straddle the Canadian and U.S. systems, view the Canadian system as unpredictable, both in fairness and accessibility. This unpredictability results in uncertainty. This not only has an impact upon American willingness to participate in the Canadian reorganization regime, but also, arguably, impacts upon American willingness to contribute to and participate in Canadian debt and equity markets. By comparison, Canadian credit capital markets are dominated by mainstream institutional lenders to the largest degree. That is, there are fewer non-bank sources of capital in Canada than in the United States, even on a relative size basis. We are speaking here of sources of private capital, such as venture capital. The importance of attracting this capital to Canadian markets should not be under-estimated and should be incorporated in the thoughts of the review by the Senate in these circumstances. Structural barriers to a flow of capital from the south to the north and from abroad include multiple securities regulation regimes, multiple personal property security regimes, multiple priority regimes and interprovincial priority regimes, and the exercise of open-ended and unpredictable judicial decision-making in reorganization cases.

All of these examples arguably impede this flow of capital to the Canadian markets and equally impede the enhancement and growth of residential and capital markets. The relative scale of the Canadian capital market to its American counterpart necessitates that Canada have that much more an efficient and accessible system than the American system in order to attract, as opposed to discourage, this flow of capital. This capital is needed within the reorganization context specifically, in order to support insolvent companies while they attempt their reorganization. The absence of this type of capital contributes to more liquidation and less reorganization, in the experience of the CBA members who debated this issue. We believe that macroeconomic issues such as these should be studied in more detail than we have been studying them to date, and that the results of these studies should be factored into your deliberations on bankruptcy and insolvency reform. This is just one example of how using these touchstones helps understand the implications of each proposed amendment. There are highlights of these recommendations that we wish to specifically draw to your attention.

We recommend the adoption of a wage-earner protection fund, sourced from a levy on employers and employees, to provide limited relief for unpaid wages in a bankruptcy situation.

We recommend that, if Parliament wishes to maintain unpaid suppliers' rights under section 81.1 of the Bankruptcy and Insolvency Act, that section should be amended to increase the notice period for the exercise of those rights to make that section more effective.

Our recommendations on governance are designed to enhance accessibility to the system, to improve the perception of independence of court officers and to level the playing field for unsecured creditors, as far as access to information and the ability to organize as a group is concerned. We would refer you to our submissions for more details on the governance submissions.

For cross-border insolvency, we recommend the adoption of the UNCITRAL Model Law, subject to modifications we identified in our written submissions.

We concur with the joint task force of the Insolvency Institute and the Canadian Association of Insolvency and Restructuring Professionals and their recommendations for the codification of debtor-in-possession financing, to entrench the right to DIP financing when certain tests are made in the legislation. However, we diverge from the joint task force submissions, in that we believe that DIP financing should be available to both large and small companies, and therefore, those rights should be entrenched in the Bankruptcy and Insolvency Act in addition to the Companies' Creditors Arrangement Act.

Because of the divergent interim receivership practices across Canadian insolvency jurisdictions, we recommend the role of the interim receiver be more clearly defined in the act, to reflect how the office is being used today. We invite you to review our corporate submissions and ask questions of us. Mr. Klotz will now introduce our submissions on personal bankruptcy and insolvency.

Mr. Robert A. Klotz, Executive Member and Past Chair, National Bankruptcy and Insolvency Law Section, Canadian Bar Association: Honourable senators, for your information I served as a member of the personal insolvency task force under Mr. Goldstein's chairmanship and I congratulate you on choosing him as your advisor. By and large, we see the task force report as a good one. In our submission, we adopted many of their proposals. I will highlight some we see as important. First, on student loans, we agree with the trustees'

organization and Mr. Stehelin, whom you have heard, that the current provisions are too harsh. I spoke before you in 1998 and said this. We recognize the financial concerns that led to the initial reform in this area. We believe that these harsh reforms have led to a new attitude in the courts and amongst students. It will effectively control the abuse problem if those measures are now made more reasonable and fairer. We believe the current law is badly designed, because it forces students who might be eligible for the court's mercy hearing to wait for ten years before having that hearing. To use an analogy, it is like being sent to jail for ten years with the right, after serving your time, to have a hearing to see if you serve the time.. That hearing should be available before, not after. It is a bad design. We said that in 1998, and we say it again. That is why we agree with the task force report to reduce the ten years down to five and to allow a one-year period after ending studies before the hardship hearing.

We agree with the task force approach to RRSP exemption. The policy goal of retirement saving is a very important goal, as is the policy favouring repayment to creditors. We believe that if money is to be preserved from creditors claims for the purpose of retirement saving, then that money should be locked in. The creditors will have the comfort of knowing that it will indeed be utilized for that socially valuable purpose and the legislation will ensure that the purpose is fulfilled. We ought not to exempt money that could be treated as a savings account and spent shortly following bankruptcy. That does not serve any goal.

Anti-collusion control is essential. Without a mandatory clawback, there is no effective remedy to control the abuse of debtors who choose to put money towards retirement that should go to unpaid creditors, be that unpaid taxes, family law property claims, or general dents shortly before bankruptcy. In our view, it is too easy to make a blanket RRSP exemption, as has been done in Saskatchewan. What is more difficult, as the task force has attempted to do, is to design an R.R.S.P. savings protection system, without bring the system into disrepute because of insufficient or inadequate anti-collusion controls. We believe the task force recommendations reflects a proper balance, subject to the minor variations indicated in our submissions.

We agree with the task force proposal to overrule implied reaffirmations, which are agreements that a debt will survive despite bankruptcy through unconscious or unknowing behaviour. However, we strongly oppose the remaining recommendation for the reasons set out in the dissent on page 32 of the English version of the task force report. For your information, that is my dissent. We see no need for the drastic change, which is ill-designed to control the problem and which significantly departs from the ethical underpinnings of our laws.

(1620, Mr. Klotz continues: ON international personal insolvency...)

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(FOLLOWING MR. KLOTZ: underpinnings of our laws.)

On international personal insolvency, we see the need and usefulness of an appropriately crafted remedy where there is no remedy available to help Canadians who filed for bankruptcy while living in the United States or another country. This is a labour mobility issue. We should not force them to go bankrupt again when they return to Canada. The task force recommendation does this effectively, with appropriate safeguards, in our view.

I shall comment briefly on a proposal which is not in our submissions or the task force report, but which has been raised before you; namely, voidable transactions. We are strongly opposed to any limitation being placed upon the trustee's right to initiate proceedings under provincial

fraudulent conveyance laws. We are also concerned that fraudulent preference legislation is amended to set up an effects-based standard. We require significant consultation and dialogue to ensure that the exceptions to such a test are properly designed to avoid injustice. Our submissions in this respect mirror those of Mr. Telfor, who made many of the same points in that respect.

Our final comments relate to the task force streamlining proposal, which we support. However, we emphasize the philosophical importance of maintaining the central role played by the trustee in maintaining public confidence in the system. If we reduce that role too much or eliminate too many of the formal proceedings in bankruptcy, we will allow an unacceptable degree of abusive conduct and strategic behaviour to slip through the system. Some of this conduct does slip through the system in any event. It is essential for the integrity of the system, and the confidence of the creditor community, not to mention the Canadian public, that the trustee plays an active and substantive role in personal insolvencies.

Senator Kelleher: Thank you, gentlemen, for being with us today. I want to ask you about the support for a scheme for workers' wage protection. We noted in the Coulter report in 1986, the advisory committee on adjustment to 89 and Bill C-22-91, each supported the creation of a wage-earner protection fund as being a fair and administratively-efficient solution.

Your specific suggestion is that such a fund be administered under the employment insurance regime and that employees be compensated for up to 90 per cent of wages for one pay period to a max of $2,000. Has anyone ever bothered to try to determine the cost of such a scheme?

Mr. Cohen: No, senator.

Senator Kelleher: Do you think that, as legislators, recommending to the government, we should have some idea of what this would cost, before we propose it?

Mr. Cohen: I think the first question for us to consider was whether it was appropriate to have some form of protection or not, because of the nature of wage-earners being captive in insolvent businesses. I think the conclusion drawn by our section of the Canadian Bar Association, the executive, and the members from across the country who joined us in that debate, was that they are a class deserving of protection.

In terms of the quantification, we viewed that the source of the funds would be from the employers and the employees and not from the government coffers, per se. In other words, it is a form of insurance like EI insurance. It is a burden on the employers and employees, but that sort of imposition of expense is necessary to protect the group that is captive in the circumstances. We support a quantification of that, absolutely.

Senator Kelleher: Do you have any expertise, any of your people, who could take a shot a trying to quantify what this might cost?

Mr. Cohen: We could go back to the labour section of the Canadian Bar Association and work with them to develop what the costs and expenses of what this would be, if the senators wish us to do so.

Senator Kelleher: Mr. Chairman, do you feel that would be helpful?

The Chairman: I guess so, sure.

Mr. Klotz: Senator Kelleher, I am not sure that we would be best suited to do this. We are lawyers not accountants. It may be that Industry Canada would be better suited to do this kind of study. We can certainly give the effort, but whether the results of our effort would be of interest to the accounting and finance people, given that we are lawyers, one might have some concerns there.

Senator Kelleher: I am aware of the limitations of lawyers. Unfortunately for you, you are here before us, and I thought I might ask. If you could take a shot at it, and even a barnyard figure.

Senator Angus: Not a barnyard, a poolroom.

Senator Kelleher: That would be helpful to us.

The Chairman: Apropos your suggestion of a fund, would that not appear to the public as an additional tax?

Mr. Cohen: It probably would appear to be an additional tax. Anything that the public has to pay is probably perceived as an additional tax.

The Chairman: I think we would have trouble recommending that. I only speak for myself.

Senator Kelleher: A number of stakeholders who have come before us have already suggested that we consider recommending legislation that would require the monitor in a CCAA reorganization to be someone other than the debtor's auditor. Others have suggested that, in the interests of saving possibly substantial sums of money, the auditor of the debtor is the person best suited to be the monitor, because the auditor already has a pretty significant knowledge of the affairs of the debtor.

Do you consider that this knowledge by a company's auditor is sufficiently useful to warrant allowing the company's auditor to be the monitor?

Mr. Cohen: I hate to say it depends. The way that we approached the issue was by saying that the monitor has to observe a standard of independence. If the monitor believes that he could not maintain independence because he was the auditor, he should recuse himself, and avoid acting in those circumstances. However, if, in the circumstances, he believes it is the best interests and nobody can come to the table with a viable challenge, then the Canadian Bar Association is not suggesting that the auditor be excluded as a monitor in the circumstances.

Senator Kelleher: We note that you recommend adoption of the UNCITRAL model law with respect to cross-border insolvency proceedings, subject to certain reservations. Your recommendation appears to indicate that it should be adopted as part of the Bankruptcy and Insolvency Act, but you do not appear to recommend that it also be adopted with respect to the CCAA, only that provisions be coordinated within the CCAA. Is this intentional or a typing lapse?

Mr. Cohen: It is not intentional to differentiate between the two.

Mr. E. Patrick Shea, Member, National Bankruptcy and Insolvency Law Section, Canadian Bar Association: Honourable senators, on page 14 of our report, the recommendation is that the CBA committee recommends the adoption of the UNCITRAL model law as part of the BIA and/or the CCAA. We leave it open as to whether it becomes part of both pieces of

legislation. As we understand, it is still open to debate whether we will have two pieces of legislation or one.

Senator Kelleher: Assuming we end up with two, would you be recommending that it become part of both?

Mr. Shea: It should become part of the Canadian insolvency process. If the entire section is included in the BIA, then reference should be had to that section in the CCAA, so that we have parallel provisions in both laws.

The Chairman: I am informed that the Human Resources Development Canada has some cost figures of what you were asking for before. So either we can call them or you can call them.

(1630 FOLLOWS - Sen. Kroft - Good afternoon. I listened...)

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(Following The Chair: call them)

Senator Kroft: Good afternoon. I listened carefully to your introductory comments, and was interested in your exhortation to us to put these specific pieces of legislation into a broader economic context. I thank you for your suggestion that we look at them to see whether they are helpful in the gathering of capital and the general workings of our economy. It is useful for us to be reminded sometimes where these issues fit in a broad economic context.

I also listened carefully with the comments about the view from the United States about the uncertainties inherent in particularly the CCAA and larger bankruptcies. It is an important area that is particularly of interest to me. Chapter 11 processes are pointed to as having a better guideline. The last point was under the dealing with contracts with labour unions.

Rather than going to one of your specific suggestions, I would ask you to elaborate a bit more on where you feel that the 22 paragraphs of the CCAA and the latitude and the flexibility that provides to the judge in the circumstance. Obviously the flipside of that is the uncertainty that you have talked about. Could you expand a bit more?

One day or another we will have one side or the other pointed to as being the advantageous approach. I would be interested in your observations.

Mr. Cohen: It is important to say that we are not suggesting that Chapter 11 is the panacea. In fact, Chapter 11 lengthens the process of organizations and is a costly way of doing things in the United States. While there are no comparative studies of running a reorganization proceeding in Canada versus the U.S., we suspect that the U.S. proceedings are much longer. We can take judicial notice of the fact that they are a heck of a lot more expensive.

We picked that example because there is some tangible evidence of forum shopping in the insolvency area. Even within the United States, between different states, there is forum shopping. Debtors choose Delaware because the Delaware bench goes out of its way to appear to be debtor-friendly. If you have only a tenuous connection to Delaware, your proceeding would be filed there.

The issue between Canada and the U.S. is different. It is not a selection of where it is debtor-friendly, although I believe that the U.S. it Chapter 11 proceedings are generally more deader-friendly. People would agree with that.

The issue between Canada and the U.S. is that we have so much a smaller piece in the economic pie in these large insolvencies, except in the obvious ones such as Air Canada, that is cantered here. We have so much a smaller piece that they would prefer to simply not deal with our system if they could avoid it rather than try to understand our system and grasp the nuances of what the judges in Toronto or B.C. might do.

That throws up an immediate barrier of the choice of Canadian forum over the U.S. forum. That starts Canadian creditors and the country as a whole on a bad footing vis-à-vis the United States.

To expand on that thought a little more I will use the anecdote of Little Rock, Arkansas. There is more venture capital found in Little Rock, Arkansas than in all of Canada. With that massive pool of money available, the lenders have a tendency to have a broader spectrum of risk.

They are prepared to take more risk in the United States. They are prepared to roll up their leaves and invest in a near-insolvent company. They are prepared to invest money and take a turn-around role. There are turn-around professionals in the United States who have, parallel to their advisory services, a venture capital fund. The turn-around specialists put their money into the company. That makes a difference. That is the real difference between the Canadian and the U.S. situations.

Senator Kroft: This is intriguing to me. Those people who are engaged in one way or another in issues of bankruptcy and insolvency are those who are in a position of those who provide the venture capital to bring the solution to the problem? It is a conjoined effort?

Mr. Cohen: The U.S. system has matured to that point. There is availability of excess cash. They are prepared to assess the risk, but in order to assess that risk and invest in that business, they participate more heavily in the process. They understand the process. It is codified. It is clear. They know that they can invest in it, and they will follow a path.

In Canada, they do not have that certainty right up front. They do not know what their footing is on the priority of the initial money that they put in because we do not have entrenched rights to debtor and possession financing, as an example. When it is done, we do not have a clear indication of the priority, and the test of the priority, of the lien that is created in respect to debtor in possession financing.

They will not put their money in at the get-go to save the business. They would not make that decision. That is a loss for the Canadian economy because the result is that the company languishes or is prematurely liquidated. There are examples.

The Canadian financial institutions do what they do very well. They lend money, and then they try and get the money back. The lending of their money is not predicated on detailed control of the businesses. They are not involved in the day-to-day operations of the businesses. Therefore, when it comes to taking a risk to debtor-in-possession financing, they may not be best served to be the one to do it unless they are already halfway into the company with much debt. They would be looking to make a bad story good.

Senator Kroft: If I can pursue the avenue that you have opened, there may be various factors in applying any public policy. Fairness and predictability are two factors. You are putting a very high premium on predictability. You would presumably be urging us to look at the entire exercise with a view to enhancing the predictability of outcome in our system.

One of the points you mentioned is the multiple jurisdictional areas. You would urge us to look for certainty of outcome in a number of these issues, and presumably at the sacrifice of something else.

I return to the flexibility or looseness of the CCAA in terms of predictability. What would you have us to do to bring more predictability to large bankruptcy situation?

Mr. Cohen: There are suggestions on debtor-in-possession financing following the joint task force report. They have done a good job of encapsulating the tests of when funding should be available that have evolved in certain jurisdictions in Canada, certainly in Ontario and other areas of Canada.

However, there is no certainty. Ontario is becoming the preferred forum for filing companies because the Ontario courts deal with that issue in a most sophisticated manner.

Senator Kroft: Judges become the attraction.

(Take 1640 Follows - Mr. Cohen: Yes. What is different...)

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(Take 1640 starts here, following Sen. Kroft: become the attraction)

Mr. Cohen: Yes. What is different, I think, from some of the submissions that you may have heard before is the people who make up the Canadian Bar Association, the lawyers who sat around the table, came from every one of these jurisdictions -- from large and small firms, from right across the country. We had representation from coast to coast, from Newfoundland to British Columbia. There was a divergence of views -- our courts do this. It is also the case in interim receivership, and I will talk about that in a second. Our courts do this in B.C. We would never get the order that you get in Ontario. Because of that, filings that could or should happen because most of the creditors are located in British Columbia might happen, in fact, in Ontario -- if there is still a sufficient connection to get over the venue tests in, for example, the CCAA.

Then they say, that is prejudicial to the small, unsecured creditors who are sitting in Nanaimo, who cannot appear in a Toronto court and cannot afford to hire a lawyer in B.C. to instruct a lawyer in Ontario to represent their interests. It also impedes the ability of those unsecured creditors to organize as a group and to collectivize so that their interests can be properly represented.

In the case of interim receiverships, it is the same issue. Interim receivership orders have evolved in Ontario, after the Curragh decision. They have evolved in Ontario to be very broad vehicles. In a recent article that I wrote for the Canadian Institute, I called it the secured creditors' CCAA -- the use of the interim receiver to obtain a stay equivalent to a CCAA stay without having to have a creditor's vote.

You can get that order in the court in Toronto. You cannot get that order in Alberta. Lawyers in Alberta lose work in the process, first of all. That is one point. That is not the thrust of our submissions, but they also lose the ability of properly represent the interests of the parties outside of Ontario.

Senator Kroft: In the macro picture, it creates uncertainties that make it difficult to get capital.

Mr. Cohen: That is right. The Americans, or even Canadians who are making proposals to invest in companies in Canada look at it and go -- I cannot invest in something that I do not know whether it has certainty attached to the outcome. Or, I am prepared to take a risk but I am not prepared to take an uncalculated risk; and I am not going to get a lawyer's opinion calculating that risk with a level of certainty that I will be comfortable with.

Senator Oliver: The one area in your presentation today that is different from some of the things that you talked about in your report is your concept of the debtor in possession. Even though the topic is bankruptcy and insolvency, this committee should be looking at a lot of other things, such as the barriers to letting venture capital and other capital come into Canada to help out at a time of debtor in possession.

GE Capital has been to Canada a number of times to help a number of companies from the United States, to provide some substantial sums at a time of possession -- so there are some American lenders already here. Even though this committee is studying bankruptcy and insolvency, are you saying that the committee in its recommendations should look outside that base core and start looking at such things as the structure of the securities' regulators in Canada?

There is already a blue ribbon committee struck by the government to do just that, so surely you are not asking us to duplicate that. How far would you like to see this committee go in making some of these more embracing recommendations to attract new capital to help out with the debtor in possession position?

Mr. Cohen: I think it is not an issue of whether you have to go outside of the sphere. What I am suggesting is that, in the context of making changes, you at least pay some homage to what the economic implications are. We can easily get wrapped up in the very partisan process of whose interests do we protect? Do we protect wage earners or trade suppliers -- do we protect this party or that party? All of that debate goes on, and that is partisan and very much a division of the pie.

What we do not necessarily do is stand back and ask if this makes us competitive. At some point in the process, we should be looking at whether this makes us competitive. When the Canadian Bar Association reviewed this, we looked at it -- and it is not our mandate, either, to improve the Canadian economy, by the way -- but certainly, we looked at it with a mind to saying, we hear enough about the inaccessibility of the Canadian system and that it is held to be suspect. We hear enough about that anecdotally to know that that is something that we do need to address.

In the context of reviewing what you have before you and the partisan issues, do not lose sight of the fact that you are making economic decisions about how competitive the Canadian economy is. In the technology of lending, as I think you have heard before, things are being streamlined and commodified below certain dollar levels. The more accessible we make our economy, and our lending and insolvency scenarios to those types of commodified practices, the more capital our country will attract. That is a significant issue, I believe.

The Chairman: Could you try to amplify this a little? I am getting slightly confused. As you have just said, our mandate here is not to figure out ways of attracting capital; but we have to be quite sure, or almost sure, that the recommendations we make will alleviate the process. Do you agree that is where we come from?

Senator Oliver: I was just going to ask him that next. When you went a little bit out on the limb, is one of your implicit concerns that, in bankruptcy and insolvency legislation, we should be looking at new and better ways of trying to save major Canadian companies, rather than just having them be wound up? If there were new and greater pools of venture capital and other capital coming into Canada -- and there were not so many barriers keeping that capital out -- would that, in your opinion, be in Canada's interest?

Mr. Cohen: We believe it would be in Canada's interests. We gave the example of the external capital attraction, but that is not the only example. It is also internal to the country, and the way that the financial institutions in Canada approach insolvencies. If we have a predictable system, we believe it will run more smoothly.

You do not want to delay it. That is the big concern about codifying, that you end up delaying it and the costs are layered on it, and that the Canadian economy cannot support that kind of cost. I do not know that we agree with leaving it completely open to courts. There are particular areas, contractual rights, which we have not actually commented on in our paper, but which have been well commented on to you. The protection or the repudiation of contractual rights in certain specific circumstances is an important issue. Financing is an important issue. Receivership is an important issue. All of those issues have to be examined in that context.

Fixing them, so that we make our system more attractive for foreign capital, improves our domestic situation as well. Keeping your eye on that ball, and making yourself more competitive vis-à-vis the world, makes you better internally as well. I think that is the point.

If you take it back one step, and you look at it from that perspective, and look at us as one sort of complete system, as opposed to a bunch of small, provincial competing systems, that is when you make the breakthrough. That is why, as you said, we stood out on a limb on that in the introduction. It was quite deliberate to draw your attention to the fact that, for the most part, we have a relatively parochial and partisan debate going on, and that it needs to be first order, not second order. We have to step back one step. That was the reason for it.

Senator Oliver: Senator Kelleher announced that two of you were his partners, trying to ensure there was no conflict. I have a similar kind of conflict question for you. You recommended that the restriction against practising lawyers acting as licensed trustees be removed. Are you not concerned that if a lawyer is acting as a trustee, that there will be a tendency for the lawyer-trustee to act as his or her own lawyer, thereby removing the level of independence, the existence of which is probably healthy in the system?

(Take 1650 follows, Mr. Shea: Our recommendation is that)

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(tk 1640 ends –Sen. Oliver… healthy in the system?)

Mr. Shea: Our recommendation is that, as a matter of licensing, there should be no restriction on a practising lawyer being able to act as a trustee. We are not advocating in any way a lawyer acting as trustee and as counsel on the same matter.

Senator Oliver: It is like on an estate if someone were to act as proctor and lawyer and executor on the same estate.

Mr. Shea: The existing rules that govern lawyers, and the rules that we are proposing in terms of independence of trustees, would prohibit a lawyer from acting as trustee and lawyer on

the same state. If he were trustee, he would have to retain independent counsel. It is also important to note that we are not advocating that lawyers could become trustees without passing the required examinations. Any lawyer that wished to become a trustee would still have to go through the required course of study and pass the examinations, but there would not be any arbitrary restriction on lawyers acting as trustees.

Mr. Klotz: Your question ties in with another one of our recommendations. That is, we note that the consumer proposal limit is proposed to be increased, perhaps to $250,000. Under the current rules, the trustee cannot use any money in the estate to hire a lawyer. If we want to encourage a trustee to take legal advice, surely we would want to encourage him to do that without him having to dip into his own pocket.

Senator Moore: Thank you, witnesses, for being here. I wanted to ask about your recommendation that the BIA and CCAA require that insolvency administrators and the debtor provide full, true and plain disclosure of every material document that is issued in an insolvency proceeding. We would have thought that, because the insolvency administrator is an officer of the court, the insolvency administrator would already be seized with that obligation.

My question is, are you aware of any specific examples where the insolvency administrator has misled creditors or has not given full and frank disclosure to creditors?

Mr. Cohen: No, we are not aware of any specific results and we were not focusing on that as a result of a specific example. We were trying in our submission to bring certainty to the system; to have a written standard of conduct in terms of disclosures, just as there is in securities regulation. You would hope that issuers of securities would also live to that standard but it is stated nonetheless. I believe a stated standard will assist trustees and monitors in attending to and addressing that issue. They can then turn to the company they act with and say, you know, this is our role and this is the scope of the role and this is the standard to which we must live according to the statute. I think it is easier for them, frankly, if they have that standard stated, to hold it out to the debtor in the circumstances.

Senator Moore: I would suggest that the superintendent of bankruptcy is in a situation to discipline those insolvency administrators who do not give complete and frank disclosure. Would that disciplinary power not be sufficient?

Mr. Cohen: They are not in a position to discipline a monitor. Only the court is in a position to discipline the monitor. The monitor is not recognized and governed by the superintendent's office. Technically speaking, they are not. In that role, they are not fulfilling a role of trustee or proposal trustee, so that is a hole.

Mr. Shea: I see the counsel to the committee is reacting. I think what we are trying to say is that, as the statute currently stands, a monitor is not required to be a licensed bankruptcy trustee prior to acting as a monitor. As a matter of practice, licensed bankruptcy trustees are appointed as monitors. If a licensed trustee were appointed as a monitor, then certainly the superintendent would have jurisdiction to discipline the trustee. The legislation, however, is separate and monitors do not have to be licensed trustees.

Senator Moore: I wanted to ask, with respect to personal bankruptcies, we note that, while you support the PITF recommendation with respect to giving some protection to RRSPs, you do not support the three-year clawback, preferring two years rather than three, and that you do not support the proposed cap.

Can you give us some indication of how you arrived at two years, rather than three? Could you provide us with your opinion as to the possibility of having a one-year clawback?

Mr. Klotz: I will give some background to that question, but, because I was a member of the task force, I will leave it to Mr. Cohen to give the more specific views. In our view, we agreed with the structure of the proposal. We agreed with the clawback. We agreed that it should be for a number of years. We agreed that it is essential to have a cheap, effective remedy because there is not an appropriate remedy that is available now.

We do not want a fraud test. The word "fraud" does not have a value in this context. We are not trying to say that anyone who contributes to an RRSP is a fraud artist. We think that is the wrong language. It is a question of policy. When someone is going bankrupt in the near future, how many years of their RRSP contributions should be paid to creditors as a matter of policy and justice? We do not think that the word "fraud" has anything to do with this issue. It is a policy question. That is why we need to have a specific number of years.

Within our group, we had divisions. There was division on the task force; the consensus was three. Within the CBA, the consensus was that two years is probably enough. That is where it stands.

By virtue of our recommendation, we do not believe that one year is sufficient. You have to remember that the bankrupt has control of the timing. In almost all cases, 99 per cent, personal bankruptcies are voluntary filings. Petitions in bankruptcy are very rare. The bankrupt has almost total control of when that bankruptcy is to be filed.

If we have a one-year period, we are allowing a degree of abuse and strategy; it is too short. Some would say that two years is two short. The CBA felt two years, on balance, was enough. The task force felt three years was enough. No matter what time period you choose, there will be some people who contribute at the end of that time period who were in fact not insolvent. We suggest that is few. With two years, it is fewer. With one year, it is not enough.

In terms of the cap, the task force noted some problems. If you do not have a cap, RRSPs, unlike pensions, can be self-administered. You raise the spectre of someone who invested their RRSP quite wisely, perhaps at MicroSoft in the 1980s, and is able to exempt a multi-million-dollar RRSP. One might say, "Good for him" or "Good for her." However, there are creditors who will be hurt. It is important for this committee to understand, as a philosophical matter, that the public will weigh this provision when we have a case where someone who may be a very bad person has injured or borrowed money from vulnerable senior citizens. The seniors have had their retirement savings destroyed but the bad person with the very large RRSP is protected. That will be something very uncomfortable to live with.

If there is no limit, then there is a possibility of this exemption putting the system into disrepute. On the whole, however, the bar association felt that the artificialities that are created with a cap are of concern. In balance, we were not convinced that the cap was appropriate. On the other hand, we felt the cap devised by the task force worked; the numbers it generated worked effectively.

You might note that the Colter commission -- I think in 1986 -- recommended a cap of $50,000. The task force cap is substantially more than that but it has the benefit of being easy to calculate and easy to apply. It generates fairly substantial numbers and we have given the examples.

We are not convinced that a cap is necessary, but if a cap is chosen, this is the way to go. Whether the cap is necessary or not is really a political judgment on what sort of contempt might be brought upon the system when we have people with multi-million dollar RRSPs facing creditors who have nothing because of the conduct of those bankrupts. That will be very hard to stomach.

Senator Angus: Good afternoon. Is it fair to say that you represent pretty fully the insolvency bar with your various committees and subcommittees? Does the panel generally embrace the practitioners' views at least?

Mr. Klotz: We have the provincial chairs who really reflect the views of their members. In addition, we have consultations among all our members. The insolvency sections provincially are fairly active.

Senator Angus: I want to follow on your interchange with Senator Kroft on forum shopping and your comment that Alberta lawyers, for example, are losing business and so on.

(tk 1700 follows--Sen. Angus cont--The current Air Canada restructuring)

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(TAKE 1700 follows after Mr. Shea - business and so on.)

The current Air Canada restructuring process is very high profile, maybe the highest profile we have ever had. A lot of Quebec lawyers are complaining about losing business due to the fact that Air Canada's head office is in Montreal, and they filed in Ontario. It has become quite a talking point. I have seen it in the media.

Do you have any comments on that? Would that be an example of inappropriate forum shopping?

Mr. Cohen: Without commenting on an active case in which I am personally involved, my firm is involved, and applying it more to a general suggestion...

Senator Angus: It is meant to be a general question but it is such a good example.

Mr. Cohen: The answer is that, in scenarios of large corporate insolvencies in the nature of Air Canada, their connections may be strong to multiple jurisdictions. It does not have to be only the strongest connection, or simply a formal connection with respect to the incorporating jurisdiction or location of head office. I could be incorporated in Delaware but carry on all my business in Ontario. An Ontario filing would be more appropriate in those circumstances.

It is very convenient for people to say, we have been hard done by because this company was incorporated here, but the filing went somewhere else. The reality is the incorporation is a mere act of formality. You have to look beyond it to see where the strong physical connection, is or where there is another strong physical connection.

Senator Angus: There could be several strong connections, and it could be wholly appropriate in one or more of these places?

Mr. Cohen: Absolutely. That is not the test in the U.S. In the U.S. you can have a plaque on a wall and you are qualified to file in that state. File first.

Senator Angus: Forgive me if you have covered the following ground. I want to get on the record what your view is. Some witnesses have suggested the BIA and the CCAA Act should be all included in one single act. Do you have a view on that?

Mr. Cohen: We do have a view. It is not stated in the report.

Senator Angus: No, I went through it again.

Mr. Cohen: It was discussed broadly. I believe the view of the group would be, and certainly we have discussed it before coming here, that it is a bit of a red herring, one or two. They both have to be right for the circumstances in which they are used. Whether you put it as two different parts in the same piece of legislation, and you have large corporate and small corporate with thresholds, or whether you have it in two separate statutes that are properly harmonized, I do not think it makes a significant difference.

Senator Angus: A bit of a red herring?

Mr. Cohen: Yes.

Senator Angus: The other question I wanted to get your view on, we have had it both ways, and you have made reference to the American provisions, chapter 11. You have made a lot of comments about cross-border insolvencies and globalization where certain industries are very much involved in a number of non-Canadian jurisdictions. I have asked other witnesses this question. What is your view, or do you have a view, on pro or con legislating for specific industries such as the airline industry or another obviously global industry that is covered already by special statute, so that this issue that we have seen in the papers lately would not come up? There is so much discretion, it seems, under the present CCAA, that there is uncertainty, and nobody really knows right now what the law is here.

Mr. Cohen: We did not debate it, and it is, therefore, hard for us to speak on behalf of the Canadian Bar Association. Thinking of it from the hypothetical standpoint, I am not sure that it makes a difference. I am not sure ...

Mr. Shea: Senator Angus was asking about dealing with an international corporation by an enacting special legislation. One of the practical difficulties with that, from a domestic point of view, is that if, by definition, the company operates in more than one jurisdiction, then enacting special reorganization legislation in Canada is not going to prevent that company from filing in another jurisdiction such as the United States, if chapter 11 is more favourable to the company's reorganization. Then are you in a situation where the company is filed in the United States, it has creditors in the United States, and how do you coordinate that with the special legislation in Canada? I do not think special legislation necessarily solves the problem.

Mr. Cohen: I was struggling with the concept of where you stop.

Senator Angus: I agree. It is a big problem. But the reality is that it seems to me, and the best example again is the current one with these labour ones and the people say, maybe Judge Farley has the jurisdiction. If we had chapter 11 they would be able to go into those collective agreements. It seems to me there is no clarity under the present law.

Mr. Cohen: I think then we fix the sections dealing with interference with contractual rights, if we believe that that is the right public policy. We fix the sections and we live with the fact that that is available to all organizations. We do not try to determine which industries this year have a bad labour situation that we need to specifically deal with.

We would make a mistake to be so narrow in the circumstances. In so doing, we are making legislation to judge a labour relationship that exists in a particular industry at a particular time. If we wish to do that, then I believe that the legislator ought to move on the Air Canada issue to legislate that issue now, if it is believed that that is an important public policy decision.

I do not believe the CBA would disagree that we should not go around looking for the industries that have that problem and go, okay, that one, and this one, and that one, we need to pre-empt. I think if it is sufficiently important, you deal with it at the time or you enact something that can be applied across the board and live with it.

Senator Angus: In other words, if it were deemed, I mean the U.S. law, I believe, is not industry specific in chapter 11. Therefore, the issue for the legislator, for the public policy here would be, do we import chapter 11 type of provisions into our laws generally or not. Is that really what I am taking from this?

Mr. Cohen: Whether we import chapter 11 or whether we look at their experience and say it is too codified, it is too specific and it clearly represents one interest over another, we make that decision, first. Then second, we move on to say, if that is not appropriate for the Canadian environment, which is admittedly different, and we like what we have here that is different from chapter 11, we are not proposing chapter 11 as a panacea. If we find there is some level of inequity that has to be dealt with, then deal with it in a Canadian way by maybe providing a specific test that has to be done or a standard that is higher, that maybe gives a little more discretion in those circumstances for the judge to act.

I know that is preaching a little bit of uncertainty out of the left side of my mouth, while we talk out of the right side on certainty, but, in some circumstances, that may be needed.

Mr. Shea: And chapter 11 is not necessarily the only model we have to go on. UNCITRAL is a good place to start looking for examples. Not the UNCITRAL model, but other UNCITRAL initiatives in insolvency are good places to start looking for an international view of best practices in the area.

Senator Hervieux-Payette: I am in favour of your getting rid of the waiting period for the Unemployment Insurance, the two weeks. I guess when you are in that situation you are not responsible for losing your job. Like my colleague, I am not favourable to the suggestion of a fund, but I was wondering, is there not a mechanism when the company does not put the money aside, stop contributing, or does some default to the pension fund, that the employee could take over the management? Very often, I just discovered when they were near bankruptcy that the company was running the whole show. Of course the employees were the ones at the end of the day. I think it was Singer in Quebec, many years later, we heard that all the money was gone with the wind.

(TAKE 1710 FOLLOWS - Sen. Hervieux-Payette continuing - If the trustee)

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(Senator Hervieux-Payette continuing - Following: the wind)

If the trustee of that fund is using the money for other purposes is there not a way of preventing that the money would not be there when needed. I look at Enron and all the people that went through the major disasters. People who are in their 60s have worked all their lives and they end up with no income or security whatsoever.

It is not happening overnight. The companies stop contributing when things turn sour. Have you looked at different kinds of mechanism? I do not know if it is a federal responsibility or a provincial one. When we make a recommendation, it should be global. How should we approach the question of having the trustee of the fund, management, not complying with certification?

Mr. Cohen: The first point is that often the horse is out of the barn. When do you have sufficient information to impose employee control over a plan? It is probably also when the provincial or federal regulatory authority could step in to deal with the issue. The money is already gone.

I do not propose to be an expert in the area of pensions but there are a number of issues that arise. Actuaries change their minds about their assumptions and then the pension fund is underfunded overnight. It is not just a matter of not contributing.

The contributions may be being made. They may not be sufficient contributions. The actuarial assumptions may be incorrect or, as has happened in the U.S., the company has access to the pension funds in certain circumstances to buy back their own stock. That is not the same case here.

The Chairman: I am not sure that is the question the senator asked.

Senator Hervieux-Payette: I understand why you are answering that, but is there a way to prevent it? You say no, because it is always too late when we learn about it or the actuary has changed his or her mind. Usually when there is a big disaster, it is due to something that has been happening for some time. If they contribute every week, the money cannot be gone the week after.

For some funds, it is only the employer who is contributing, However, most of time it is the employer and the employee. The employees have that deduction on their paycheque. Week after week it has to be sent to a certain place. Should they not monitor that and see what is happening with that more often than every five years?

The Chairman: That is not a bankruptcy though.

Senator Hervieux-Payette: When the bankruptcy arrives, we are caught with the problem that all these people do not have their pension fund. It is one of the major problems in bankruptcy.

The creditors will loose some money. People who have lent money will lose money. People losing their job and all their savings and pension is the greatest damage of bankruptcy to me.

The Chairman: Is that to be examined under the question of how do you look after pension funds?

Mr. Klotz: I was about to say something to the same effect, Mr. Chairman. Bankruptcy interacts with provincial laws. Administration of pensions, particularly if it is a provincial pension, should be dealt with by the pension board in that province. It does not matter whether there is a bankruptcy, reorganization; the company stops carrying on business or is happily carrying on business and be underfunded. The provincial pension board, if it is a provincial pension that should be monitoring that.

I am not sure if this committee can address that issue. It is an important issue, I would agree. It relies on properly functioning provincial legislation, and I presume that with federal industries, federal pension legislation as well.

Senator Hervieux-Payette: You will make the recommendation to make a fund at the provincial level? You say that there should be another fund where people would contribute and administer. You say that that is a federal authority.

I have some problem with that. I am of the same mind as my colleagues. I do not want to add another level of administration and another contribution to all the workers.

Mr. Cohen: We anticipated that concern because of issues such as Enron, senator. You will notice that the recommendation on the wage fund differs from the recommendation on the unpaid pension fund.

It says that the CBA recommends that if Parliament wishes to provide protection to contributors of unremitted pension contributions in bankruptcy, it should do so in a similar fashion to the wage earners.

We were not recommending that it be done. We were saying that if you think it is fit and appropriate for federal government to impose a protection in the circumstances, then the model to use is the wage earner model as opposed to a priorities model running ahead of secured creditors, for example.

I do not mean to pass the buck. You have raised an important issue, but we were not measuring the relative importance of that interest in the circumstances. We were saying that if Parliament wishes to do it, then this is the way we would recommend it be done.

That differs from what we are saying in the wage earner recommendation. In that case we are saying that it should be done. That is the distinction.

The Chairman: You might have in the CBCA some kind of clause stating that as part of the yearly audit, the auditors report on the condition of the pension plan. It seems to me to worry about the pension when bankruptcy is declared is too late. The cat is out of the bag.

Mr. Cohen: I would agree.

Senator Kroft: I want to raise a question that arises from a news report last week regarding the enormously complex settlement of the WorldCom affairs. Apparently as part of that settlement and apparently based on the provisions of the new Sarbanes-Oxley Act, with which this committee has become familiar, they have agreed under the framework of this law that shareholders will get $500 million U.S. The number is not important but it appears that from the attempts to bring corporate rationality in post-Enron shareholders will have rights in a bankruptcy situation ahead of creditors, which is the point of this report.

I know that we have to be compatible and attractive to the Americans, but it also works the other way around. I did not know if you had any sense of this. I am really leaning on you on both this subject and the other one. Have you any awareness of this? Is there any parallel discussion happening in this country? Does this come as a complete surprise to you?

Mr. Shea: In the context of a Canadian insolvency proceeding, typically shareholders do not receive anything for their shares. We are not aware--

Mr. Cohen: There was one scenario in the second Eaton's reorganization where in order to convey the tax losses to Sears when the business was sold, they had to convey the shareholdings of the company to allow the Eaton's entity to be amalgamated with Sears. In that way, the tax losses could be used to offset Sears' profits.

Senator Kroft: Presumably that was a mechanism for another purpose. It was not a cash transfer.

Mr. Cohen: It was a requirement of Sears in the purchase that they kept the shares so that they could avail themselves of the tax clause. I acted for probably one of the largest creditors in the Eaton's scenario. It sat sour with us that the shareholders got a $20 million note that was paid on the never, never plan. They were not sure if they would be able to take advantage of the tax losses. I think that they were quite sure. If they were able to take advantage of the tax losses, they would pay on the note.

(Take 1720 Follows - Mr. Cohen continuing: They immediately took advantage...)

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(1710 precedes, Mr. Cohen: would pay on the note.)

(1720, Mr. Cohen continuing)

*** They immediately took advantage of the tax losses and I think Eaton's shareholders got almost $20 million. Mr. Justice Farley commented on that in a number of decisions on Eaton's, but he said there was no other game in town if you wanted that deal at that dollar level from Sears. It provided a lot more money going to the unsecureds than in a liquidation scenario, where Sears was buying the skeletal remains. You had to pay to get the shareholder cooperation. Whether $20 million was the right amount of money or not, I leave open for other people to assess. I will not tell you my personal view on that. That is an anomaly within the Canadian context.

Senator Kroft: You have confirmed that point, that conceptually and in principle, it would be foreign to the Canadian context. However, you have also made a secondary point, which is that it attests once again to the incredible flexibility of the CCAA that Justice Farley can again leap over that principle and that broad fundamental of our law, in order to make an accommodation on the basis that it was the only game in town.

Mr. Cohen: He had the ultimate word in the sanctioning, but before that, the unsecured creditors voted and approved. It was in a plan and it was a 99 per cent approval level. CCRA abstained from voting and there were a few trade creditors who declined. It was voted on in those circumstances because, in fact, it was the best scenario.

Senator Kroft: It may be arising out of an agreement with the creditors here as well, but I was interested in your reaction.

Mr. Cohen: I think there would be a pretty strong negative reaction to shareholders' interests being served in that way.

The Chairman: Thank you very much for your excellent presentation.

Our second witness is not only from the International Insolvency Institute, but, I am told, is the founder. He is a pioneer in formulating the international Model Law on bankruptcy. Before you tell us anything, please accept our congratulations, sir.

Welcome to the committee. I assume you have an opening statement.

(1730 follows, Mr. Leonard: I have a brief opening statement)

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(Following The Chair: opening statement)

Mr. Bruce Leonard, Chairman, International Insolvency Institute: I have a brief opening statement.

Thank you, honourable senators, for the invitation to appear today. I appear on behalf of the International Insolvency Institute, which despite its name, is actually a Canadian non-profit corporation.

The goal of the institute is to gather the leading academics, judges and regulators from around the world into a single forum where we can concentrate on improving international systems and procedures. It is a limited membership organization. We are limited to 150 members from around the world. At the moment we have about 40 countries in or membership. We try to have the outstanding practitioners and judges from each of those jurisdictions join us in our work.

We are a fairly young organization. We are only three years old, but we show seasons of being here for the long-term.

In terms of material for the committee, I believe you should have all received a copy of the English version of the written submission from the institute. My apologies to the senator for not having the French version available. I had promised Mr. Robert that I would deliver succinct remarks, but I broke my promise. I said I would deliver them in a timely fashion, and I broke that promise, too. He has not been able to obtain the French translation yet, but it will be around shortly. I apologize for my tardiness.

You should have received also a CD with source material on international insolvency. It brings together in a single place material that is not available anywhere else. I hope everybody has access to a CD ROM because it has good source material in it for deliberations. Everybody should have received a copy of the UNCITRAL model law with the guide for enactment.

Thank you Mr. Robert for getting those arrangements done in a timely fashion.

I will break my opening remarks into two segments. The first is Canada's place in the world and our need to coordinate our systems with the systems of our major trading partners. How does Canada fit into the international scheme of things?

Second, how does Canada compare competitively in its domestic insolvency procedures with our major trading partners?

Part one of my remarks will focus on the UNCITRAL model law and our very strong recommendation that this committee consider recommending its adoption in Canada. A little bit of background to the model law would probably be in order.

UNCITRAL stands for the United Nations Commission on International Trade Law. It is the United Nations commercial arm. It is headquartered in Vienna. Over the pat 30 to 40 years, since the Second World War, UNCITRAL has prepared a number of model laws, conventions and statutes that have been recommended to countries in the United Nations.

I asked External Affairs to give me a short note on how many UNCITRAL conventions Canada has adopted. I have not heard back from them yet. There may be six or eight UNCITRAL creations that Canada has formally adopted. This would be another one of that series.

UNCITRAL began this project in 1994. The object of the project was to increase the ability of insolvency representatives in different countries to access the courts of countries where their debtor had assets. This is multinational organizations and insolvencies.

Prior to the early 1990s, there were very few international reorganizations. The dominant theory internationally at that time was territoriality. Each country took jurisdiction over the assets of a company within its jurisdiction and would not share or cooperate, by and large, with other countries that had other parts of the same company's assets.

The UNCITRAL model law was derived as a means to try to allow international coordination in insolvency and reorganization cases because everybody involved in the process recognized that having a business as a going concern always added value over having a business liquidated. Stakeholders in each country would benefit from having the business reorganized successfully as a whole, instead of being torn apart by individual proceedings in individual jurisdictions.

The UNCITRAL model law involved consideration by 60 countries. Canada was prominent in the deliberations that led to the development of the model law. The chair of the UNCITRAL working group that produced the model law was a lawyer from the Department of Justice. Canada was very prominent in the development and promulgation of the model law.

The model law received approval from the United Nations in late 1997. As far as any of us know, that is the fastest project that the United Nations has ever had. It was three years start to finish.

What is the model law? It is a system. It is a framework for cooperation. It is not intended to change anybody's substantive legislation. It is more procedural than substantive. It sets up a framework so that international reorganizations and liquidations can be coordinated to preserve value for the stakeholders of the companies that run into financial difficulty.

International acceptance is quite good. The United States has had a version of the model law on its books since 1998. It has been part of their bankruptcy reform process. That process has been hung up with a number of extraneous issues that you would just not believe unless you followed the U.S. process.

At last count, the various houses of Congress had passed the model law seven times. That is sincerity. It has been passed seven times, three in the house and four in the Senate. It falls into sessional breaks without passing both houses.

Senator Oliver: Where is it now?

Mr. Leonard: That is a very good question. It was passed most recently by the House of Representatives in this current session and has gone to the Senate. It has not been controversial. I am expecting that the Senate will pick it up. There will then be a conference between the Senate and the House, and it will get passed by both houses this time. However, I have said that before.

Other countries have adopted it. The first major country to adopt it was Mexico. Mexico took it pretty much as is and put it into their bankruptcy law in 2001. South Africa has also

passed it. However, the III member in Johannesburg has informed me that for some reason that he does not understand, the South African legislation has not been proclaimed into force yet.

Remarkably, Japan has passed a variant of the model law. Japan is a civil law country with territorial jurisdiction. Prior to the model law, they would not recognize foreign insolvency proceedings nor would they extend the effect of domestic proceedings abroad. For Japan to recognize the law and incorporate it into their legislation is truly a remarkable event.

In England, legislation has been passed to enable the adoption of the model law. Australia has produced a report recommending the adoption of the model law. I have checked with a III member on the progress of that legislation. They expect to have the model law in place in their country later this year or early next. New Zealand has prepared a report recommending adoption of the model law, and it is expected to be adopted there as well.

The last country on the list that UNCITRAL sends to me is Eritrea. It has passed the model law.

(Take 1740 Follows - Mr. Leonard continuing: They count. They have...)

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(Take 1740 starts here, Mr. Leonard continuing - passed the model law)

*** They count. They have a vote at the United Nations just like we do.

Senator Kelleher: Is there anybody there with any money?

Mr. Leonard: The Eritrean experience seemed to be connected to a project involving the U.S. agency for international development.

Senator Oliver: The U.S. has a big base there.

Mr. Leonard: That would be the logical conclusion. I think the model law has received a high level of international acceptance. If the Americans pass it, I think the Brits will. I think they are waiting for the U.S. to make the first move.

If you include England, the United States, Mexico, Japan and Australia, by themselves -- the people who have indicated that they are prepared to or have passed the model law -- when you put all those people into one group, I think it becomes almost imperative that Canada join in that system to incorporate the model law into both of its statutes as part of the overall insolvency framework in this country.

Questions have been raised as to whether the interests of domestic Canadian creditors are protected when you adopt the model law, and the answer is that they are protected. The reference in the III brief is on page 11. In any adoption or application of foreign insolvency proceedings, the model law indicates that the interests of domestic creditors are to be taken into account.

The adoption of the model law would not amount to an abdication of any kind of Canadian responsibility. Canadian courts would still be able to take care of Canadian creditors. I just commend the committee to the references and to the text of the model law.

On the CD ROM, we have the Australian report, the New Zealand report and the U.K. act that allows the adoption of the model law. Hopefully, this will be of some assistance to the committee in its deliberations.

In terms of briefly commenting on where Canada fits into the world, in terms of domestic competitiveness of its insolvency system, at this juncture, the submissions are that Canada's system is in drastic need of overhaul. I commend this committee very much for its interest in the topic.

This committee, over the years, has spent more time and attention on insolvency reform than most other committees. I remember being here in 1996 in connection with the 1997 amendments, and I think I recognize some of the faces from that appearance. In my view, this committee is probably the last chance that Canada has to have acceptable, modern insolvency legislation.

It has been a legislative orphan all the way along. Nobody is paying much attention to it. However, it is tremendously important framework legislation and it deserves a better ride than it has had in Parliament to this point.

I would like to sum up the criticisms that have been levelled, primarily at the CCAA internationally, in four points. Then I suspect my four points will elicit some questions, so I will then defer to them.

In my view, and in the submissions of the III, the Canadian system lacks transparency. There seems to be -- and I am sorry to say this -- a lack of integrity in the system. There certainly seems to be a lack of predictability in the system; and it is almost beyond question that there is a lack of success in our system in reorganizing companies.

I thought that would provoke Mr. Goldstein. It may well do.

I hope that is enough to stimulate some questions and I will amplify upon my remarks in responding to them if I may.

Senator Oliver: I will leave questions about transparency, integrity, predictability and success to others. I would like to ask why you are limited to 150 members. You said you have 40 members now, but that you have a cap of 150. Where was that imposed from? Is there a statute?

Mr. Leonard: No, it is self-imposed -- insolvency being the peculiar discipline that it is.

Senator Oliver: Why could it not be 151?

Mr. Leonard: It could. It is an arbitrary number because insolvency is a peculiar discipline that is not likely to have mass appeal. There was a certain cachet to being one of only 150 members in the world to an organization. It has proved successful. I think as we expand and take on other tasks, we will probably enlarge the membership.

Senator Oliver: I just could not understand that. Thank you for that answer. Second, you gave the names of a number of countries -- U.S., U.K., Mexico, Japan, South Africa, Australia, New Zealand, Eritrea and so on -- who like your code, and some have partly adopted it. In terms of Canada, the main thing you are asking this committee to do is to recommend adoption to the Government of Canada.

Would you consider it appropriate to stipulate in the model law that it would be applicable to foreign representatives in Canada only if the country from which they come has also adopted the model code, or has bankruptcy and insolvency provisions substantially the same as ours?

Mr. Leonard: No, but I can elaborate on the answer. That is really a very live issue. South Africa, in fact, adopted a reciprocity provision -- over the disagreement of the people who did their report.

To explain my answer, let me go back to the current provisions of the BIA and CCAA that were adopted in 1997. In 1997, the UNCITRAL model law was almost done. There were a few more meetings to be held. There was a small subcommittee established in 1997, which I was privileged to co-chair, to deal with international provisions.

At that time, what we did in that committee -- and our recommendations pretty much verbatim made it into the BIA and the CCAA at that time -- we looked at the UNCITRAL model law and said this looks like where UNCITRAL is going, so let us pick up these principles and put them into our legislation. Parliament in the fullness of time adopted that. We have the current provisions because that is where UNCITRAL was at the time.

Subsequent to our having to go to Parliament to have the act amended in 1991, the UNCITRAL process concluded in a manner that no one had anticipated. The real answer is that the delegate from France, who had been slowing the process down for -- I should not be critical -- the delegate from France who had been raising a lot of interesting questions about the process suddenly bought into the picture. There was a tremendous international consensus that developed suddenly, which produced a more well-formed view of international cooperation than we were able, at that time, to get into the act.

We did not go for reciprocity at that time, so the Canadian system, as it exists now, does not require reciprocity. The Canadian system for recognizing foreign insolvency proceedings basically says, okay, if the foreign insolvency representative is validly appointed in a proper proceeding in his country, we will recognize him. We are not asking for a quid pro quo. It just seems fair, if he is authorized and able to deal with the business...

Senator Oliver: I think there should be a quid pro quo. I think there should be reciprocity.

Mr. Leonard: I am not sure it is an exercise of sovereign rights. It is a commercial...

Senator Oliver: Earlier you said, does not worry, Canadian domestic creditors will be protected. What if a large company had domestic creditors in South Africa, Mexico, Japan and the United States, and also had some in Canada? Will there be any priority for how these creditors will be protected, or will it be identical to the way that the foreign creditors will be protected? Will Canada's creditors receive any sort of priority?

(Take 1750 follows, Mr. Leonard: The answer to that is)

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(TAKE 1750 STARTS HERE following Sen. Oliver: sort of priority?)

Mr. Leonard: The answer to that is, if the Canadian creditors were inclined, the model law allows them to start a domestic Canadian proceeding. The assets in Canada would be administered in a domestic Canadian proceeding.

Senator Oliver: It would cover assets only in Canada and not in the in other jurisdictions such as in South Africa or Mexico?

Mr. Leonard: That is the deal. There is an overall international umbrella for the organization as a whole, but for domestic assets, those are dealt with on a country-to-country

basis internally. There will be only one master proceeding. If there is an international asset, the master proceeding takes the international assets, but the domestic creditors are able to exercise their rights under their domestic legislation.

Senator Oliver: But they cannot get anything internationally? If there were more international assets in Japan or Mexico or South Africa, you are saying that Canadian domestic creditors could not benefit from that in any way?

Mr. Leonard: Not if there was a domestic Japanese proceeding. We take the UNCITRAL model law, its progress on the international level, a step at a time. The model law is an advance over where we were, but it is not the end of the story. Ultimately, if you want to get to the fairest system to all creditors, it would be to have one administration treating all creditors evenly.

Senator Oliver: That is my point.

Mr. Leonard: The politics of the UNCITRAL system were such that we could not get there in the first phase. That would be something that we would ultimately try to work to. We were not able to get there the first time. It was enough of a miracle to get what there was, we are grateful for that, and we will work on improving it. We are getting there but we are not where you think we should be. I think we should be there too, but we are not there yet.

Senator Kroft: You have provided irresistible temptations with that last list. I thank Senator Oliver for resisting that temptation. I will not attempt all of them, but I will pick two.

Let us start with what you mean by integrity.

Mr. Leonard: By integrity, I mean conflict of interest, primarily conflict of interest. There are no rules in the CCAA for conflict of interest.

We have insolvency administrators with multiple positions, multiple responsibilities, and what bothers me is that some of the multiple responsibilities are conflicting. It is not just the auditor being the monitor, which is the first instance of a conflict of interest, which -- well, it was statutorily enshrined in 1992.

Parliament bought into the argument that we would save a lot of money if the auditors who already knew about the business could be the monitors. Prior to the 1992 amendments, there had been cases in which the courts had disqualified firms from acting as monitor, informally because it was not in the legislation. Firms had been disqualified because they were the auditor, and it was an obvious conflict. In 1992, Parliament bought into the argument that you would save a lot of money if you used the auditor to be the monitor. So it was put into the legislation that that could happen, but that does not excuse the conflict.

When you get to other countries, they cannot believe that we have a statutorily enshrined conflict of interest like this. There it is. Our recommendation would be that that should be revoked. That is for starters.

The next series of conflicts is that the monitor often acts as either the financial advisor to the debtor, or the financial advisor to the secured creditors.

The monitor who is appointed by the court is supposed to be fiduciary to all the creditors and they all say they are. Then they take on these multiple representations where they can act for creditor A, who has an inconsistent interest with creditor B, but they are also acting for creditor

B. It gets worse because sometimes when a plan fails, the monitor is first in line to say, I can be the receiver.

Another area of conflict is that the receiver owes his obligations primarily to the first secured creditor, but as monitor, he is also acting for the unsecured creditors, and as auditor, he is acting for the shareholders of the company. It gets too complicated for words.

My recommendation would be that we go to the one-hat theory. Could everybody involved in a CCAA organization, please only wear one hat?

Senator Kroft: I do not want to reveal myself as naive in your eyes, but why do you think that you are the first witness, to my knowledge, who has raised this point?

Mr. Leonard: I can only speculate. If it has not been raised at this committee, it has certainly been shouted about enough at professional gatherings. I would be alarmed if my comments were a surprise to the committee. Some of my background involves U.S. practice. I have been involved peripherally in the U.S. legislative process. I believe I am the only Canadian member of the National Bankruptcy Conference in the United States, which is a non-profit organization that makes submissions on improving U.S legislation. So I see how their system works. They have a test called disinterestedness. If you are going to be appointed as an insolvency administrator, or a professional advisor in a U.S. case, you must pass the test of being "disinterested," which means, when you take on a position, you do that job and you do not do other jobs. Your interest is directed to your constituency and you are not to share it, divert it, act in manners that are inconsistent with the interests of the people you are appointed to represent. In Canada, under the CCAA, there are no restrictions, so you have insolvency administrators wearing two, three, and occasionally, four hats. Who are they responsible to? How do they carry out their responsibilities?

The other point I would make, in response to a very good question, is that you might be able to live with a system like that if there were any independent creditor representation in a case.

In the BIA, the legislation contemplates a board of inspectors that are supposed to advise the trustee-in-bankruptcy. The CCAA should, and this is part of our recommendations, provide for creditors' committees so that the people who have the investment in the situation are able to organize themselves and make their views known to the monitor, to the court and so on. However, there is no provision in the act for the creditors to be represented in that fashion. It is as if the CCAA has gone out of its way to squeeze whatever remnants of creditor democracy slopped over from the BIA entirely. Under the CCAA, you have rely on the monitor.

The monitor, of course, usually has these conflicting responsibilities. The other disadvantage of the monitor system, since I am on the topic, is that the monitor should be responsive to the needs and wishes of the creditors. Monitors almost never call meetings of creditors. They must divine the wishes of the creditors by osmosis, because they never ask for the views of the creditors. Nobody elects a monitor. It is a bad situation. It cries out for reform. That is why I say there is a transparency issue.

There was a question earlier about whether these monitors make full, true and plain disclosure. I would differ a little from the answer given by the Canadian Bar Association and I would say: Occasionally they do. There is no question that sometimes they do. That means that sometimes they do not.

One of my best examples is a major CCAA cross-border case. I cannot because of the record tell you what it is but I can tell you afterwards. There was a monitor appointed. This is a major case out of Toronto, from where most of the CCAA problems seem to emerge.

(TAKE 1800 FOLLOWS - Continue Mr. Leonard - This is a)

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(1750 precedes, Mr. Leonard: most of the CCAA problems seem to emerge)

(1800, Mr. Leonard continuing)

**** This is a company with a turnover of hundreds of millions of dollars a year. Partway through the case, I raised my hand and said, "Please, sir, can we have a report on how the business is doing? We are a substantial creditor. There was no creditors' committee. How can we find out what is going on? You are our eyes and ears." The monitor, a national firm represented by a national law firm wrote back through counsel, saying, "We do not have an obligation to report to you. When we go back to the court next, we will report, but in the meantime, there is nothing in the statute that requires us to report to you. Stop bothering us."

Being the good-natured person I was, I did not take offence; however, it is not a great system.

Senator Kroft: You have hinted at that and I understand your reticence.

How do you measure success? What measurements or standards do you use do you use to measure success?

Mr. Leonard: It is subjective. There is no real test of measuring success. I take success as the debtor entity reorganized in sort of the same condition that it was before, maybe with different ownership, maybe not, but carrying on in substantially the same form as it entered the proceedings. That is success.

Let me make another contrast with the U.S. to explain my comment. The U.S. system is based on the "fresh start" principle. They believe, as an article of faith, that a company that runs into financial difficulty should have the opportunity to make a fresh start. There are historical reasons for that, but that is their theory.

We inherited from England a respect for people who lend money. Our system promotes a rapid and efficient realization on assets in an insolvency case. Our system, with its short timeframes, no creditor participation, and insolvency administrators who have varying loyalties, promotes sale of assets. Our system does not seem to be intended to promote reorganizations. A successful CCAA, I will give you another example of this, is a quick sale of the assets to an American company.

One of the largest manufacturing concerns of its kind in Canada last year went into a CCAA. You would think that that was going to lead to reorganization, recapitalization, some sort of rescheduling of debt or conversion of debt to equity. No, that is not the Canadian way. Within 60 days of it having gone into CCAA, the monitor had organized a sale, as a going concern, of the assets to a large American company. There was, of course, no creditor participation in the system, apart from the creditors that held first security on the assets. The monitor went to the court and said, "Look, if we can sell this business to this huge American company, we can save a number of jobs and the business will continue."

The assets were sold to the American company in a fairly short timeframe and life goes on. It is now a subsidiary of an American company carrying on, but the company is dead. The creditors who had money in the company got nothing and the shareholders, of course, were wiped out. That is a typical Canadian reorganization.

I think we, as a country, do better. We need some motivation to do that.

Senator Kelleher: I get the feeling that you would urge upon us the adoption of the Model Law here in Canada. Is that a fair statement?

Mr. Leonard: Yes.

Senator Kelleher: Do you have any further reasons you would like to give us for that?

Mr. Leonard: Thank you; that is a good question. I think if Canada adopted the Model Law, we would probably stem or at least slow down the flow of Canadian reorganizations that are going to the United States. For that, I guess I have to back up. There are half a dozen cases in the last two or three years of major Canadian companies reorganizing in the United States. You ask yourself why that is. Is our system not adequate to handle our reorganization? Of course it is. Apart from the other things I have mentioned about predictability and lack of success, why do they go down there? Leeuwen went to the United States and reorganized and is now an American company with a head office in the United States. Laidlaw is now an American company, or will be when it emerges shortly. Livent went down to the United States. Philip Services, a decades-old company in Hamilton, is now a company in Chicago.

Why do these people do that? I think they saw some advantages to the U.S. system in how they could reorganize. There is a recommendation in the brief, because one of the things that all those companies shared was a liability of securities class actions against them. In the United States, securities class action claims are treated as equity. In Canada, they are treated as debt. This distinction meant that they could not reorganize successfully in Canada, so they had to go to the United States.

If the UNCITRAL Model Law were in place, and if it is passed by Congress one more time, UNCITRAL recognizes, or the Model Law recognizes, a proceeding that is taken in the "centre of main interests" of the reorganizing company. That is a European term, but it means the head office jurisdiction. If the UNCITRAL had been in place in Canada and the United States when Philip Services, Laidlaw and Leeuwen filed, the U.S. would recognize the Canadian proceeding. You would not need to go into the United States. If that will help us reorganize Canadian companies in Canada, I think that is a worthy objective, apart from the other more general comment that anything that promotes an international reorganization rather than an international liquidation is a good thing, because it maintains more stakeholder value.

Senator Kelleher: One final question, Mr. Chairman. To your knowledge, have other countries that have adopted the UNCITRAL Model Law inserted provisions that protect local creditors first?

Mr. Leonard: The Model Law, in the references on page 11 of the report, does itself contain provisions that say that the courts must have regard to the interests of domestic creditors in applying the Model Law. So anyone who has applied the Model Law or adopted the Model Law as a text would have that protection built in.

Senator Moore: Are they given priority, though?

Mr. Leonard: Priority is tougher. Are they given priority over other creditors?

Senator Moore: Are domestic creditors given priority over other creditors?

Mr. Leonard: In a sense they are; however, it is not under that provision. Where it comes from is that the Model Law allows domestic proceedings to take place and the domestic proceedings then govern.

Senator Moore: Have any of the countries that have adopted it put in a proviso that their domestic creditors come first?

Mr. Leonard: I do not think so. There are local preference clauses. With France and labour claims, you will never get them to back off labour claim priorities. Those kinds of things cannot be dealt with.

The Chairman: Thank you for being with us. It was interesting and we appreciate your candour and your information.

(1810 follows, The Chairman continuing: Our last witness of the day)

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(The Chair continuing: Following: information)

Our last witness of the day is an individual witness. Mr. Bob van Leeuwen. President of van Leeuwen Engineer Limited. I understand you have an opening statement.

Mr. Bob van Leeuwen, President, van Leeuwen Engineering Limited, As an Individual: I have a set of slides, which I believe you have a copy of. Essentially I am here to help try to reduce the number of bankruptcies and also to try to reduce the effect of bankruptcies when they happen. My title is "Ethics, Profits and Taxes - Increase Profits through: Ethical Credit Relationships, More Efficient Transactions."

I will give a background on ethics. From my perspective, bad debt is approximately a $10 billion a year problem in Canada. Fraud is about $25 billion a year. These are my estimates backed up by other people's estimates. The global default rate is estimated by Standard and Poor's at 3.499 per cent. Their analyst is Diane Vazza. That is pretty close to the 3.5 per cent that I estimate for Canada for the combination of bad debt and fraud -- $35 billion out of a one trillion dollar economy.

I will be talking about transaction costs and whether they are appropriate. The cost of electronic money currently is about two per cent of revenue, should you decide to use it, and that is most commonly available in the form of a credit card. You may be aware that credit cards cost businesses in the order of 1.5 to 5 per cent of revenue. The smaller you are, the higher the percentage.

My uncle started the first credit card company in the Maritimes, possibly in Canada. I know a little bit about the credit card business. I know a little bit about where it comes from and where it is going.

I am asking for two things. One item is a provincial responsibility and the other is federal.

Under provincial responsibility, I am asking for establishment in law of something which I call a partial security interest or a shared security interest. This would allow you to share the first, second or third interest in a piece of property with a number of creditors. This would have

to be structured, obviously, in the same way that banks have to use a structured approach when they give you a line of credit against your house.

It would allow you to have multiple credit relationships using the same piece of security. It would be of benefit in terms of allowing smaller debts to be secured, which would reduce bad debt.

I have a transaction instrument with a one-pager that we can cover a little bit later that should help in fraud reduction by giving a period to the transaction. This particular instrument, if used properly, would allow interest cost reduction for all firms because you would be using credit instead of real money.

On the federal level, I am looking electronic money. It is a generic term. I am basically looking for a port for a financial institution that is not a bank to plug into the Canadian Payments Association.

That is important because if you want competition in transaction methodologies, you need to be able to be a small start-up, plug into the electronic payment system and grow. It is very difficult to be a small start-up and be asked for $5 million in deposits -- a $20,000 deposit to apply to be a member of the CPA and all the infrastructure and continuing costs of that.

(Take 1820 Follows - Mr. van Leeuwen continuing: Just as all new computers have...)

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(tk 1820ends--Mr. van Leeuwen cont--costs associated with that.)

Just as all new computers have a USB port, I think there ought to be a new port on the Canadian Payments Association where small, start-up, financial-transaction companies can plug in and try out their methodologies. If they grow, they can either eventually migrate to being a bank or, if the committee decides, some other form of structure.

The reason that you would want electronic money, from my perspective, is for paperless monetary exchange, for distance monetary exchange, and for removal of a key e-commerce barrier. I view this as about a 0.1 per cent GDP improvement and an efficiency improvement. It is actually a zero-cost or 100-per-cent efficiency improvement. If we look at profit level – and we will look at that a little bit later -- it ends up being a 10-times factor for profit improvement.

On profits, I believe partial-security interests would help reduce bad debt and fraud, which cost companies approximately 3.5 per cent of revenue. If we use an artificial value of 10 per cent profit for an average firm -- I understand from the Canadian Payments Association that 10 per cent is actually a fairly good number for the average Canadian profit level in Canadian corporations -- we would be looking at a 35-per-cent potential improvement in profit levels for Canadian corporations. For electronic money, a 0.1-per-cent GDP increase would therefore increase profits by approximately 1 per cent.

If you are looking at profits, obviously there is a tax implication. If your profits are 35 per cent higher, your taxes would be 35 per cent higher. There is actually a fairly good economic benefit to the government for implementing this kind of thing.

From discussions that I have had with the Bank of Canada, they are doing an initial study on this at a very high level. I interpret that to mean, "We might do this in ten years if we are lucky." However, there is a little bit of agreement that it is just a matter of time before we have some sort

of electronic money in Canada, so that I can transfer $50 to my son's electronic wallet from my electronic wallet.

Without going into how those things might be used a little bit better, maybe you want to ask a few questions?

The Chairman: Can you tell us how this affects bankruptcy?

Mr. van Leeuwen: Maybe I will use the visual aid that I borrowed from my son. In bankruptcy, all the creditors are in line. You service the first creditor or the first security interest first. Then the other creditors get their turn. I am suggesting that a partial security interest would allow creditors to choose to be at the front of the line by sharing a security interest.

For example, I have a line of credit against my house with a zero balance owing. I am a mechanical engineer. If I want to buy an injection-moulding tool, it might cost $16,000 and take 20 weeks to deliver. If I wanted to order one of those things right now, I would have to give the money up front because the moulding company will not believe that I am creditworthy. If I had a partial security interest, I could effectively give him the same interest in my house that a construction lien would give him, if he were a construction company. He could therefore see that I am creditworthy. I would not have to write the cheque until I actually got the tool. That would save me 20 weeks' worth of interest. These days, that is not as significant a saving as it was a few years ago. It is still a cost and it is one that I would like to avoid.

The Chairman: What does this have to do with bankruptcy?

Mr. van Leeuwen: In bankruptcy law, you are looking at different sorts of interests. The Canadian Apparel Federation has asked for a different kind of interest for their membership. The Canadian Labour Congress has asked for a priority interest. The Ottawa Airport Authority has asked for reservation of a priority interest for airport improvement fees. All of these things are done with what I would call micro-payments. In other words, the payments are less than $150,000 and they are serial; in other words, there is a stream of these payments.

The only way you can guarantee that kind of thing at the present is with a letter of credit. Letters of credit are incredibly difficult to implement. I am talking about something that would be essentially as easy to use as a credit card but which would give you a secured interest in a piece of property. It allows you to become a secured creditor when, otherwise, in bankruptcy, you would not be considered one.

The Chairman: To be perfectly blunt about it, we are having some trouble with your presentation. You obviously have a level of intelligence beyond mine because I do not understand it. My adviser does not understand it.

Mr. van Leeuwen: I have been an unsecured creditor, as has my dad as has his dad before him. When you get into bankruptcy as an unsecured creditor, you are left unsatisfied pretty well 100 per cent of the time. The only way a company like mine, which provides engineering services, can ensure that it gets paid by a client in bankruptcy is to get a security interest. At present, I cannot get a security interest so that I am assured of that process in bankruptcy as a secured creditor, unless it happens prior to bankruptcy.

The Chairman: You would get your security interest by this joint payment guarantee instrument?

Mr. van Leeuwen: The joint payment guarantee instrument would be a way to supply that, yes. However, it does not need to be done that way. It could be done just by issuing a partial security interest through the local property office on Elgin Street, in the Ottawa court house.

The Chairman: What does this have to do with electronic money?

Mr. van Leeuwen: The electronic money is a way to provide these kinds of services with financial firms. I believe your committee is also looking at ways to stimulate competition in the insurance and banking industries.

The Chairman: Wait, you are way off.

Mr. van Leeuwen: It is another subject.

The Chairman: You can say whatever you want but you are going into a whole other realm.

Mr. van Leeuwen: This is a contingency trade credit instrument that allows you to have a claim in bankruptcy as a secured creditor, where you otherwise would not have one.

Senator Kroft: Suppose there is a piece of security that would get "shared," in your language. You talked about registering that security at the property office; would that be like a land titles registration, for instance? Would the mechanism allow a charge against that asset through an existing mechanism, like a land titles office or other property registration? Or are you looking at creating something new to manage this?

Mr. van Leeuwen: There are two ways this could be managed. One is through the land registry office. However, if it was the bank of the buyer that issued this partial security interest, they could also manage that within their own purview. The issue, on a legal basis, as I understand it, is that the need to register the security with the property office in order to have it as a legal registration.

Senator Kroft: Let us not complicate it. Let us say, instead of a house worth $100,000, that you had $100,000 cash. You want to use that to leverage your credit or support your credit as much as possible, so you give your bank the $100,000 cash. The bank holds it. Then you want to order your injection moulder and do some other things.

Mr. van Leeuwen: Effectively this would clear the amount of the cheque before the cheque was written.

Senator Kroft: So the bank would set aside the agreed-upon amount. Perhaps you are allowed to purchase merchandise worth up to 75 per cent of your asset. The bank would put a claim of that amount against your $100,000 until you had used up to the 75 per cent leverage level?

Mr. van Leeuwen: Right.

The Chairman: Excuse me, is that not identical to a letter of credit?

Senator Kroft: That is what I was getting to, Mr. Chairman.

You said earlier that the only way of achieving this now is through a letter of credit, which is a complex thing to do. If I want to establish a letter of credit, I have to do just essentially what I have described, plus I must pay a fee to whoever is establishing the letter of credit to have it confirmed -- or not confirmed -- and to go through other processes.

Really that is what we are talking about. You want to add on to that a delivery mechanism through this card system.

Mr. van Leeuwen: The delivery system that I am talking about makes it different from a letter of credit and also different from escrow; yet it is similar to both of them. The distinction between this suggestion and a letter of credit is that, once a letter of credit is issued, the seller is paid as soon as the invoice is issued. There is no way for the buyer to stop that from happening. You cannot disrupt that process. A letter of credit is inviolable once it has been issued.

With this suggested instrument, if the invoice is sent but the buyer does not sign off as being satisfied, then the purchase amount is put into a joint account controlled by both the buyer and the seller. The funds cannot be dispersed unless both the buyer and the seller agree. That would make it something like escrow but not exactly like it. The reason it is not exactly like escrow is that it would only be issued to the account once there was a problem, whereas, when you create an escrow account, you create it prior to any transaction.

The Chairman: Mr. Van Leeuwen, I am going to give your submission and this one-pager to our consulting and expert staff at the Library of Parliament to see if they can explain it to me and to our committee.

If we need further explanation, we will come back to you. Thank you for being with us. This meeting is adjourned.

The committee adjourned.