The Incremental Evolution of National Receivership Law and the Elusive Search for Federal Purpose

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Introduction

There was a period when provincial legislation that trespassed too deeply into the federal field of bankruptcy and insolvency law was likely to be declared to be *ultra vires* as an invasion of the exclusive federal power in relation to that field.[1] The five-to-four split in the 1978 Supreme Court of Canada decision in *Robinson v Countrywide Factors Ltd*[2] was very much a turning point. Thereafter, the constitutionality of provincial legislation was almost invariably determined through the application of the paramountcy principle.[3] Pursuant to this principle, a provincial statute is rendered inoperative to the extent that it conflicts with the federal statute. The Supreme Court of Canada has created a two-branched test for determining the presence of a conflict. Under the first branch, there is an operational conflict when it is impossible to comply with both the federal and the provincial statute.[4] Under the second branch, there is a conflict when the operation of the provincial statute frustrates the purpose of the federal statute.[5] Either type of conflict will render the provincial statute inoperative.

In November 2015, the Supreme Court of Canada in *Saskatchewan (Attorney General) v Lemare Lake Logging Ltd*[6] considered a constitutional challenge to provincial farm protection legislation on the ground that it conflicted with federal legislation that empowers a court to appoint a national receiver under the *Bankruptcy and Insolvency Act* (*BIA*).[7] The first branch was not engaged since the secured creditor could comply with both federal and provincial laws by waiting the longer period and satisfying the more stringent provisions of the provincial statute. The matter therefore fell to be decided on the basis of the second branch of the paramountcy principle.

Determining purpose and objectives has not proven difficult in the case of the long-standing and established federal insolvency systems. For example, the purpose of the bankruptcy system has been described in a series of Supreme Court of Canada decisions.[8] However, the federal receivership provisions are of a different character. Justice Côté described the process that has given rise to these provisions as "an incremental evolution."[9] The search for a federal purpose behind them has proven to be more problematic. The Supreme Court of Canada in *Lemare Lake* undertook this search. The majority decision brings into question the relevance of one of the fundamental dynamic elements of receivership law and casts doubt on whether it should be characterized as a federal insolvency system at all. In this article I will seek to explain how and why this has come to pass.

The Background

3L Cattle Company Ltd. (3L Cattle) had given a security interest to Lemare Lake Logging Ltd. (Lemare Lake) in its land and in its goods other than inventory to secure an obligation. Following a default, Lemare Lake applied to the Saskatchewan Court of Queen's Bench for the appointment

under the *BIA* of a national receiver of the assets of 3L Cattle, excluding the livestock. 3L Cattle argued that the court was required to dismiss the application because the procedural requirements of the *Saskatchewan Farm Security Act*[10] (*SFSA*) had not been satisfied. Lemare Lake argued that the provisions of the *SFSA* were inoperative by virtue of the principle of federal paramountcy.

The *SFSA* imposes significant procedural hurdles on a secured creditor who seeks to enforce its security. It prohibits any action against farm land unless a court order is obtained. The creditor cannot apply for the order until after the expiry of 150 days, and a mandatory review and mediation process must be engaged.[11] A court is required to presume that the farmer is making sincere and reasonable efforts to satisfy the obligations and must dismiss the application if the secured creditor fails to rebut this presumption.[12] Even if the secured creditor satisfies this burden, the court may still dismiss the application if it is satisfied that it is not just and equitable according to the purpose and spirit of the *SFSA* to make the order.[13]

Compared to the *SFSA*, the receivership provisions in the *BIA* are more of a legislative patchwork. The original bankruptcy statute did not govern receiverships at all. In 1992, the Act was amended with the addition of Part XI respecting receiverships.[14] These provisions were very much focused on problems associated with privately appointed receivers — the lack of accountability to anyone other than the secured creditor who made the appointment, and the very short period of time that was afforded to the debtor before the receiver took over control of the debtor's business. Section 244 of the *BIA* required a secured creditor to give a notice of intention before enforcing its security interest, and prohibited enforcement until the expiry of ten days after the notice.

Curiously, the concept of a national receiver did not originally emanate from these provisions. Instead, it first came about when courts used their authority to appoint an interim receiver.[15] Although the legislation envisaged a narrow and limited watchdog role under which the interim receiver would preserve the status quo and ensure that the assets were not dissipated, courts seized upon the wording of the section that allowed the court to "take such other action as the court considers advisable."[16] Courts used this as the basis to appoint a national receiver who was given the same broad powers that were afforded to court-appointed receivers to operate the business and to undertake a going concern sale.[17] The orders also sought to relieve a receiver of liability under environmental legislation and successor rights legislation, but subsequent judicial decisions rendered this approach untenable.[18]

The 2009 amendments to the *BIA* institutionalized this emerging practice of appointing a receiver under federal legislation. It returned the interim receiver to its original limited role, but created a new power of appointment that authorized courts to appoint a receiver under the *BIA*. The statute incorporates the traditional "just or convenient" ground for the appointment of a receiver and empowers the court to authorize the receiver to take possession of the assets, exercise control over the assets and the business, and to take any other action that the court considers advisable.[19] A number of additional provisions were added. A qualification requirement was added so that only a licensed trustee can be appointed as a receiver,[20] and the application was required to be filed in the judicial district of the locality of the debtor.[21] The court was also authorized to create a charge ranking ahead of any or all of the secured creditors for the fees and disbursements of the receiver.[22] Beyond these scant provisions, the substantive law was not to be found in legislation, but rather in the decisions of courts that supervised court-appointed receivers.

The Supreme Court's Search for Federal Purpose

A party who challenges legislation pursuant to the second branch of the paramountcy principle is required to establish the purpose of the federal statute and to show that the provincial legislation is incompatible with this purpose. It was abundantly clear that the 2009 amendments were intended to codify the practice of the fed-

eral appointment of a receiver that would be recognized throughout Canada, thereby avoiding a multiplicity of proceedings. The critical question was whether this was the only purpose of the 2009 amendments, or if they also implied the idea that receivership proceedings were intended to give rise to a timely and efficient avenue for enforcement of a security interest.

The Attorney General for Saskatchewan argued that its purpose was simply to permit the appointment of a national receiver who could act throughout Canada. *Amicus* maintained that its purpose was to create a body of substantive federal receivership law that was uniform across Canada and that was built upon the concept of timeliness and real-time responsiveness. The decision in *Lemare Lake* ultimately turned on the methodology through which this federal purpose was to be determined.

The decision of the majority was delivered by Justices Abella and Gascon. They held that the narrow purpose of section 243 of the *BIA* was to establish a regime for the appointment of a national receiver in order to eliminate the need for multiple appointments in other provincial and territorial jurisdictions. The ten day waiting period established only a minimum waiting period and it did not preclude the creation of a longer waiting period under provincial law. The majority thought that the idea of timeliness inherent in the idea of "real-time" litigation had developed in relation to restructuring law under the *Companies' Creditors Arrangement Act*, but that it was not to operate as a more general norm in bankruptcy and insolvency law. They stated that "[a] judicially coined phrase, however magnetically phrased, that describes judicial practices in the context of restructurings, can hardly be said to be evidence of the legislative purpose of a national receivership regime."[23]

The sole dissenting view was that of Justice Côté. She thought that the federal provisions were "intended to establish a process for appointing national receivers that would be effective, timely, capable of responding to emergencies (or, in a word, flexible) and sensitive to the totality of circumstances."[24] She also thought that the ten day notice period signalled the need for urgency and real-time decision-making that is central to the effectiveness of receivership proceedings.

Both the majority and the minority sought to shore up their respective positions by finding support in other provisions of the *BIA*. The majority thought that elements of urgency were part of the design of the reformulated interim receiver provisions and that the absence of an equivalent feature in section 243 indicated that this was not a feature of the national receiver. The dissent thought that the thirty day time limitation on interim receivers indicated that Parliament intended that a nationally-appointed receiver was to be appointed promptly. The majority thought that the discretion given to a court to make an appointment showed that a secured creditor was not entitled to the appointment of a receiver and that provincial interference with a discretion granted under federal law was not enough to establish frustration of federal purpose. The dissent thought that the existence of the discretion simply highlighted the need for the court to be responsive to the particular factual matrix on a case-by-case basis. The majority thought that the special treatment afforded to farmers in other federal insolvency systems showed that Parliament thought that it was appropriate to afford special treatment to farmers by not subjecting them to the ordinary bankruptcy and insolvency processes. The dissent thought that the federal treatment of farmers showed a concern for time sensitivity that was wholly absent from the provincial legislation.

Gradualism and the Evolution of National Receivership Law

Parliament has enacted a number of statutes that create insolvency systems. The bankruptcy system is the best known, but there are several others such as the *Companies' Creditors Arrangement Act*[25] (*CCAA*). In almost all instances, it is possible to identify the exact moment in time when the federal insolvency system came into existence. So, for example, the bankruptcy system was created on July 1, 1920 upon its coming into force after its enactment the previous year, and the *CCAA* was created in 1933 in the

midst of the Great Depression. Moreover, the identification of the purpose of these insolvency systems is not a difficult exercise. There are often extensive Parliamentary debates and other background documents that provide considerable detail on these matters.

But there is one insolvency system that proves an exception to this rule. There is an emerging body of national receivership law that has its source in the provisions of the *BIA*. But these provisions are not comprehensive in scope and one must look to the common law and equity to find the governing substantive principles that animate receivership law. Justice Côté's description of this body of law as "the product of an incremental evolution" is apt, as her analogy conveys the idea of gradualism; it is difficult to discern a federal purpose in the same way that can be done with all the other federal insolvency systems.

In evolutionary biology, the idea of gradual and incremental change explains why it is not possible to pinpoint with any precision when the first member of a new species evolves. There never was a first whale or a first bird. Every creature is born of the same species as its parent. It is only after many, many generations that the incremental changes have compounded to such an extent that we would conclude that the descendent is no longer of the same species as its distant ancestor.

This idea of gradual and incremental change can help us understand why it is so difficult to identify the purpose behind the federal receivership provisions when this does not prove so difficult in respect of the other insolvency systems. Unlike the other insolvency systems that have an objective that is publicised, discussed, and debated, the federal receivership provisions are gradually giving shape to a new insolvency system. And as with other types of gradual change, it is difficult to assign any particular date to when this change came about. There are two elements to this incremental growth of federal receivership law: first, the legislative amendments to the *BIA* that introduce increasing federal regulation and oversight of receiverships; and second, the development of judicial norms and practices that put meat on the bare bones of the statute.

The legislative developments first began with the federal regulation of receiverships in 1992 and followed up with the 2009 amendments. Viewed in isolation, the statutory provisions in Part XI of the *BIA* do seem to lack the comprehensiveness of many of the other federal insolvency systems. It is undoubtedly true that the receivership provisions of the *BIA* contain very little in the way of substantive provisions. For example, there are no rules that govern the stays of proceedings or the operation and sale of the business under receivership.

Viewed from a broader perspective, the idea that receivership proceedings constitute a federally regulated insolvency system is more plausible. The *BIA* amendments have increasingly extended the statutory repossessory rights and charges to receiverships as well as the other insolvency systems.[26] The section 244 ten-day notice is integrated into the *BIA* restructuring regime in that a debtor who is given the ten day notice can immediately respond by giving a notice of intention to file a commercial proposal.[27] This initiates restructuring proceedings and automatically gives rise to a stay of proceedings. The 2009 amendments to the *BIA* gave licenced trustees a monopoly on receivership engagements, but also resulted in the federal regulatory oversight of receivers.[28] Clearly, this body of law is being increasingly drawn into the federal orbit.

Moreover, the insolvency law statute is not the source of the most important rules in receivership proceedings. The applicable law is found in the practices and the decisions of courts that are using the federal provisions. The stay of proceedings, the powers of the receiver, and many other important matters are found in the court orders. The development of template receivership orders[29] in provinces that have formal or informal commercial lists occurred under the former interim receiver provisions of the *BIA*, and have continued following the 2009 amendments. The vast majority of court appointments are authorized under the federal provision. It is difficult to square these developments with the idea that the sole purpose of the federal appointment of a

receiver was simply to permit the appointment of a national receiver who could act throughout Canada. Federal receivership appointments were routinely used both before and after the 2009 amendments when the debtor did not have extra-provincial assets.

It is in the practices of the courts in hearing receivership proceedings that ideas of urgency and timeliness are most strongly encountered. And it is here that the majority decision of the Supreme Court of Canada is most out of step with the day-to-day activities of insolvency lawyers and judges. The majority suggests that timeliness and real-time responsiveness to changing dynamics are aspects of restructuring law, but are not animating features of receivership law. The idea of real-time litigation refers to the sensitivity to time that is necessary when delays can rapidly erode asset value. Real-time litigation is operationalized in two ways: through the special supervisory role of the judge who will hear several applications from the commencement of the proceedings to their conclusion; and, through the unique role of the insolvency practitioner who serves as a court officer (the monitor, trustee, or receiver) and provides the court and the creditors with critical information. Although the idea of real-time litigation was first developed in connection with restructuring proceedings, insolvency lawyers and professionals now recognize that these are more generalized insolvency law norms that guide the commercial list judges in all insolvency proceedings. Indeed, with the advent of the liquidating *CCAA*, there has been a blurring of the differences between restructuring and receiverships that further supports the application of the norms to both receivership and restructuring proceedings without differentiation.[30]

Future Implications

The contrast between the treatment of federal receivership law with the development of the law under the *CCAA* is most interesting. This statute was also initially characterized as skeletal in nature. Courts began to make orders that altered the legal rights of those who dealt with the insolvent company. Although there was initial uncertainty concerning the source of this power, it was ultimately justified as being grounded in the statute itself; it operated in a gap-filling role where the statute was intended to achieve a particular purpose but no statutory mechanism was provided to achieve it.[31] The federal statute was thus regarded as a bare framework that permitted the creative judicial development of a wide range of orders that altered the rights of those who dealt with the company. The Supreme Court of Canada in *Sun Indalex Finance, LLC v United Steelworkers*[32] held that provincial legislation that conflicted with a court order made under the *CCAA* was rendered inoperative by the paramountcy doctrine.

Why is it that the skeletal framework of the *CCAA* was expansively interpreted so as to permit the making of orders that conflicted with provincial legislation, but the same argument has fallen flat in the case of the federal receivership provisions? One might argue that there is a clearer legislative framework to the *CCAA* and more in the way of extrinsic evidence of Parliamentary intention. But, it may also be that the remarkable free-wheeling judicial attitude that spawned the creation of restructuring law has come to an end. The judicial development of restructuring law occurred at a time when any hope of insolvency law had ground to a standstill.[33] Canada had no effective insolvency system that could be employed to rescue a financially distressed company at a time when a sharp recession brought many companies to the financial brink. Much has changed since. The periodic amendment of bankruptcy and insolvency law is now the norm, and courts may now be less inclined to take on a role that might be seen by critics as activist or legislative in nature. The authority to make the wide-ranging orders of past have now been codified in the *CCAA* and this further supports the expectation that it is for Parliament to legislate on such matters.

This shift from judicial development to statutory codification means that the same moves that worked in incremental judicial development of the *CCAA* are not going to succeed in the realm of receivership law. The idea that the power given by a court to "take any other action that the court

considers advisable"[34] allows a receiver to override valid provincial legislation is now simply off the table. In *Railside Developments Ltd. (Re)*,[35] the Nova Scotia Supreme Court held that the authorization in the *BIA* did not permit a court to override provincial legislation that requires the consent of encumbrances in order to register property as a condominium. The decision of the Supreme Court of Canada in *Lemare Lake* almost certainly confirms this to be the case.

Lemare Lake has likely had its greatest impact in the province of Quebec. The Civil Code of Quebec (CCQ), sets out rules concerning notice periods that must be given by a secured creditor prior to enforcement.[36] It was widely thought that the federal receivership provisions operated as a code that overrode the need for compliance with these provincial notice requirements if the federal receivership route was taken.[37] *Lemare Lake* has challenged this assumption, and may greatly limit the use of the federal court appointed receiver in Quebec.

A truly national body of receivership law will now need to be fashioned by legislation. There are several good reasons why this legislation might be expected to come about. The existing skeletal approach is highly problematic in the province of Quebec, and this is compounded by the fact that the equitable principles that are used by common law courts to fill in the gaps is foreign to the civil law tradition of Quebec, thus resulting in an untenable exceptionalism. The widespread use of the commercial proposal as a substitute for receivership proceedings[38] illustrates the need for an insolvency system that codifies the operative principles so as to create a better fit with Quebec's civil law tradition. Moreover, the current legislative framework that governs receiverships is fragmentary and confusing. It preserves archaic distinctions between privately appointed and court appointed receivers that are out of step with modern realities.

Admittedly, codification would be a bold step. It would mean the abandonment of the present incrementalism in favour of drafting and designing a new part of the *BIA* that would seek to comprehensively set out the fundamental principles of receivership law. It would fully recognize receivership law as an autonomous insolvency system on par with the other established federal insolvency systems. In doing so, it would permit the creation of a truly national and uniform body of receivership law throughout Canada in which the objectives of the system would be articulated and the balance between the need or timeliness and compliance with provincial enactment could be directly addressed.

Endnotes

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1 *Reference re Debt Adjustment Act, 1937 (Alberta),* [1942] SCR 31, 1 DLR 1 (provincial debt adjustment legislation found to be *ultra vires*); *Canadian Bankers' Association v Attorney-General of Saskatchewan,* [1956] SCR 31, [1955] 5 DLR 736 (provincial moratorium legislation found to be *ultra vires*); *Reference re Validity of Orderly Payment of Debts Act, 1959 (Alberta),* [1960] SCR 571, 23 DLR (2d) 449 (provincial orderly payment of debts legislation found to be *ultra vires*).

2 [1978] 1 SCR 753, 72 DLR (3d) 500 [*Countrywide Factors*].

3 A quintet of Supreme Court of Canada decisions, which applied the paramountcy principle to resolve conflicts between provincial law and the bankruptcy scheme of distribution, followed closely on the heels of *Countrywide Factors, ibid*. See *Deputy Minister of Revenue v Rainville*, [1980] 1 SCR 35, 105 DLR (3d) 270*; Deloitte Haskins & Sells Ltd v Workers' Compensation Board*, [1985] 1 SCR 785, 19 DLR (4th) 577; *Federal Business Development Bank v Quebec (Commission de la santé et de la sécurité du travail)*, [1988] 1 SCR 1061, 50 DLR (4th) 577; *British Columbia v Henfrey Samson Belair Ltd*, [1989] 2 SCR 24, 59 DLR (4th) 726; *Husky Oil Operations Ltd v Minister of National Revenue*, [1995] 3 SCR 453, 128 DLR (4th) 1.

4 *Multiple Access Ltd v McCutcheon*, [1982] 2 SCR 161 at 191, 138 DLR (3d) 1.

5 *Canadian Western Bank v Alberta*, 2007 SCC 22 at para 73, [2007] 2 SCR 3; *Bank of Montreal v Hall*, [1990] 1 SCR 121, 65 DLR (4th) 361.

6 2015 SCC 53, [2015] 3 SCR 419 [*Lemare Lake*].

7 RSC 1985, c B-3, as amended by *Wage Earner Protection Program Act* SC 2005, c 47, s 115, and *An Act to amend the Bankruptcy and Insolvency*

Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, SC 2007, c 36, s 58 [*BIA*].

8 *Industrial Acceptance Corp v Lalonde*, [1952] 2 SCR 109, [1952] 3 DLR 348; *Vachon v Canada (Employment & Immigration Commission)*, [1985] 2 SCR 417, 23 DLR (4th) 641; *Alberta (Attorney General) v Moloney,* 2015 SCC 51, [2015] 3 SCR 327.

9 *Lemare Lake*, *supra* note 6 at para 95, per Côté, J.

10 SS 1988-89, c S-17.1 [*SFSA*].

11 *Ibid* s 12.

12 *Ibid* ss 13, 18.

13 *Ibid* s 19.

14 *Bankruptcy and Insolvency Act*, RSC, 1985 c B-3, as amended by SC 1992, c 27.

15 *BIA*, *supra* note 7, s 47.

16 *Ibid* s 47(2)(c).

17 *Canada (Minister of Indian Affairs & Northern Development) v Curragh Inc* (1994), 114 DLR (4th) 176, 27 CBR (3d) 148 (Ont SC).

18 *GMAC Commercial Credit Corporation - Canada v TCT Logistics Inc*, 2006 SCC 35, [2006] 2 SCR 123; *Re Big Sky Living Inc*, 2002 ABQB 659, 37 CBR (4th) 42.

19 *BIA, supra* note 7, s 243(1).

20 *Ibid* s 243(4).

21 *Ibid* s 243(5).

22 *Ibid* s 243(6).

23 *Lemare Lake, supra* note 6 at para 41.

24 *Ibid* at para 82.

25 RSC 1985, c C-36.

26 *BIA, supra* note 7, s 14.06(7), ss 81.1 to 81.6.

27 *Ibid* ss 50.4(1), 69.

28 *Bankruptcy and Insolvency General Rules*, CRC, c 368, ss 34-53.

29 For a discussion of template receivership orders, see Roderick J Wood, *Bankruptcy and Insolvency Law,* 2nd ed (Toronto: Irwin Law, 2015) 507-08.

30 See D Bish, "The Plight of Receiverships in a CCAA World" (2013) 2 J of the Insolvency Institute of Canada 221.

31 *Century Services Inc. v Canada (Attorney General)*, 2010 SCC 60 at paras 64-65, [2010] 3 SCR 379.

32 2013 SCC 6, [2013] 1 SCR 271.

33 See Thomas Telfer, "Canadian Insolvency Law Reform and 'Our Bankrupt Legislative Process'" (2010) 1 Annual Rev Insolvency L 583.

34 *BIA, supra* note 7, s 243(1)(c).

35 2010 NSSC 13, 95 CLR (3d) 54.

36 CQLR c CCQ-1991, arts 257 and 278.

37 *Re 9113-7521 Québec Inc (Syndic de)*, 2011 QCCS 3429, 83 CBR (5th) 66. See also C Lachance & H Babos-Marchand, "The 'Impractical Effect' of *Lemare Lake Logging Ltd*. In The Enforcement of Security in Quebec" (2016) 28 Commercial Insolvency R 25.

38 Statistics gathered by the Office of the Superintendent in Bankruptcy in the Insolvency Statistics in Canada — Annual Reports from 2010 to 2015 indicate that 70% of all the commercial proposals that are filed by artificial entities originate in Quebec.