

# Options for mid-sized businesses

## Management issue paper

Over the last few years a number of high profile companies in Canada have filed for bankruptcy protection under the Companies' Creditors Arrangement Act (CCAA). The latest is Air Canada. Do smaller companies have similar options?

The CCAA provides a special mechanism that allows companies to make formal compromises with their creditors and it enables a company to "stay" the creditors' ability to press for payments. The Bankruptcy Court determines whether or not a company's application for relief under the CCAA is acceptable. If it is accepted, the Court oversees the process and ultimately approves or disapproves the formal plan that the company works out with its' creditors. During the process the Court often hears a number of applications for consideration of specific issues that arise during the process such as the provision of new financing to allow the company to continue to operate.

Of major importance, however, is that the CCAA is only available to companies who owe creditors in excess of \$5,000,000. Is there something available for companies who have liabilities of less than \$5,000,000? Fortunately, the answer is, yes.

The Bankruptcy and Insolvency Act (BIA) has provisions for an insolvent company, to file a Division 1 Proposal with creditors.

A Division 1 Proposal through the BIA is available to any insolvent company regardless of their liabilities are greater than \$5,000,000. However, for larger companies, the CCAA is much more flexible than the BIA's provisions for proposals.

The aforementioned Proposal is a plan of compromise and arrangement for creditors. If the plan is unacceptable to the creditors, then the company is deemed to be bankrupt under the provisions of the BIA. However, if a successful proposal can be implemented, the company will realize an opportunity to reduce its exposure to its creditors that can allow it to go forward with an improved balance sheet.

To file a Proposal, a company must meet stringent filing requirements under the BIA. There are specified timelines for the filing of cash flow projections and for the filing of the terms of the proposal. The BIA specifically addresses the issue that: all creditors are to be informed; and a meeting of creditors to vote on the terms of the Proposal must be held within a specific timeframe.

Managing a company through a proposal process can be difficult. Its greatest limitations are the necessity to finance and continue operations during the proposal period and, then the need to fund the proposal if it is successful. The filing of a

Proposal is a clear notification that the company is insolvent. Once suppliers are informed, they will obviously be reluctant to provide further credit. Because of this, it will become necessary to organize funds to pay C.O.D. for supplies to keep the operations open.

How much will be required and how you can provide for these funds, is a major hurdle for many companies.

Under the CCAA, a business must also fund its continuing operations. In some cases, lenders may offer to provide funding to larger companies in exchange for improved security provisions. Debtor In Possession (DIP) financing can be found if a company has a solid asset backing to offer as security and if the Court will give the new funds priority over current debt. For smaller companies, it is often much more difficult to find this type of financing under a Proposal.

Another issue is the professional costs involved. Under a BIA proposal, the costs a smaller company can accrue are a consideration. However, it can often be managed. The procedures under the BIA are less expensive than those under the CCAA. Take for example Air Canada, which is involved in a large compromise arrangement – it had over 100 lawyers at some of its court appearances. Smaller companies requiring a proposal will often only need the singular company lawyer and a trustee.

Having to utilize any of these two procedures is never a pleasant time for those involved. The CCAA and the BIA are two solutions that will formally allow a company to present a plan of compromise and arrangement to their creditors. These arrangements may

allow the company to survive and go forward, as their creditors are often willing to support a viable plan. After all, no one wants to lose any business.

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