



BALANCING INTERESTS: AN OVERVIEW OF THE WAGE EARNER PROTECTION PROGRAM

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Introduction

Some say that the Canadian government was almost prescient when it introduced the *Wage Earner Protection Program Act*² (“WEPPA”) in 2005. Designed to provide employees with better protection for unpaid wages in the face of the insolvency of their employer, WEPPA could not have come at a better time for Canadian employees when it was proclaimed into force on July 7, 2008, amidst the global economic crisis.

Prior to WEPPA, wage earners traditionally fared very poorly in the face of an employer’s bankruptcy. Although they ranked as preferred creditors in respect of amounts owing for wages and pension benefits, wage earners typically received little to no compensation for wages earned in a bankruptcy. The introduction of WEPPA and related amendments to the *Bankruptcy and Insolvency Act*³ have dramatically changed the landscape for wage earners by giving them priority status to a portion of their claims for unpaid wages and unpaid pension contributions. However, this protection has come at the expense of the priority typically afforded to lenders and other secured creditors. It has also increased the costs of administering a bankruptcy or a receivership.

¹ With thanks to Patrick Déziel, an articling student at Miller Thomson LLP, for his capable assistance in preparing this article.

² *Wage Earner Protection Program Act*, S.C. 2005, c. 47, s. 1 [WEPPA or the Act].

³ *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 [BIA].

This paper provides a brief overview of WEPPA and the amendments to the BIA, the key elements with respect to wages and pensions, the mechanism of the Wage Earner Protection Plan (the “WEPP”) and the impact these changes have had on insolvency proceedings and secured creditors.

WEPPA: How it Works from the Employee’s Perspective

Eligibility for Unpaid Wages

WEPPA protects employees in the event of a bankruptcy or a receivership by allowing them to claim eligible wages up to \$3,000 (or four weeks worth of insurable earnings under the *Employment Insurance Act*⁴, whichever is greater) if:

- (a) The individual’s employment ends for a reason prescribed by regulation⁵;
- (b) The former employer is bankrupt or subject to a receivership; and
- (c) The individual is owed eligible wages by the former employer.

WEPPA does not apply to employees whose employer has filed for protection under the *Companies’ Creditors Arrangement Act*⁶ [CCAA].

How Does it Work?

The WEPP is administered by the Minister of Labour through Service Canada⁷. In order to make a claim under the WEPP, employees are required to submit an application⁸ for payment no later than 56 days after the later of:

⁴ *Employment Insurance Act*, S.C. 1996, c. 23.

⁵ According to section 3 of *Wage Earner Protection Program Regulations*, SOR/2008-222 [WEPPA Regulations], an individual’s employment has ended if it has ended for the following reasons: (a) the individual resigned or retired; (b) his or her employment has been terminated; and (c) the term of the employment has expired.

⁶ *Companies’ Creditors Arrangement Act*, R.S.C. 1985, c. C-36 [CCAA].

⁷ Claims may be made online at the Service Canada website, which also contains a variety of other pertinent information: <<http://www.servicecanada.gc.ca/eng/sc/wepp/index.shtml>>.

The bankruptcy or receivership;

The end of the applicant's employment; and

The receiver terminates the applicant's employment.⁹

Beyond submitting an application, the claiming employee is not required to engage in any part of the bankruptcy process. Applications are submitted on-line by the employee through Service Canada.

Eligible Wages

Eligible wages are defined in the Act as wages earned during the six months prior to the date of bankruptcy or the date of the appointment of a receiver.¹⁰ "Wages" includes salaries, commissions, compensation for services rendered, vacation pay, severance pay, termination pay,¹¹ gratuities, disbursements for travelling salespeople, production bonuses and shift premiums.¹²

In *Ted Leroy Trucking Ltd. and 383838 B.C. Ltd. (Re.)*,¹³ one of very few cases to have substantively discussed WEPPA since its inception, the court considered the meaning of the phrase "compensation for services rendered" in the context of its application to the portions of wages paid directly to third parties. In this case, the issue was union dues that were paid directly by the employer to the union pursuant to a collective agreement. The British Columbia Supreme Court noted the expansive definition of "wages" contained in the Act and held that it included not only amounts paid directly to the

⁸ *WEPPA Regulations*, s. 10

⁹ *WEPPA Regulations*, s. 9.

¹⁰ *WEPPA*, s. 2(1).

¹¹ *WEPPA*, s. 2(1).

¹² *WEPPA Regulations*, s. 2

¹³ *Ted Leroy Trucking Ltd. and 383838 B.C. Ltd. (Re.)*, [2009] B.C.J. No. 8 (B.C.S.C.) [Ted Leroy].

employee but also “other amounts that were earned by the employee and which were directed to be paid to a third party by the employee [...]”¹⁴

Statutory Deductions

Payment on any entitlement to a claim will be automatically reduced by 6.82% as prescribed by the *WEPPA Regulations*. They will also be reduced by “any amount that the individual has received after the date of the bankruptcy or the first day on which there was a receiver in relation to the former employer by virtue of his or her rights in respect of the eligible wages.”¹⁵

Review

Section 9 of the Act provides that the Minister is responsible for determining if an applicant is eligible for payment under the WEPP. Where an applicant wishes to challenge the Minister’s determination, the Act contains review mechanisms, whereby an employee may request a review of the Minister’s decision regarding his or her eligibility within 30 days of being informed of the eligibility determination.¹⁶ An appeal from this review before an adjudicator (appointed by the Minister) may be requested within 60 days of being informed of the review decision.

Ineligible Individuals

Certain individuals with wage claims are ineligible to receive payments under WEPPA. These include officers and directors, persons with a controlling interest in the business, persons who occupied a

¹⁴ *Ted Leroy, ibid.* at para. 22.

¹⁵ *WEPPA Regulations*, s. 6.

¹⁶ *WEPPA*, s. 11 and *WEPPA Regulations*, s. 11.

managerial (as defined by the *WEPPA Regulations*) position, and persons who did not deal at arm's length with officers, directors, persons with a controlling interest or managers.¹⁷

Employee Wage / Termination Issues

Recovery of termination and severance pay was not initially part of WEPPA. These categories of "wages" were added to the Act effective January 27, 2009¹⁸ and serve to increase the amount claimable by employees who are entitled to compensation pursuant to provincial employment standards and other legislation. Generally speaking, employees who are terminated without cause or notice and who have worked for their employer for a given length of time are statutorily entitled to pay in lieu of notice.¹⁹ It appears that an employee's entitlement to pay in lieu of any common law notice period will not be included in the term "termination pay" for WEPPA purposes.²⁰

Interestingly, while these categories of payments were added to expand the types of claims eligible under the WEPP, they are not included in the \$2,000 super-priority charge on current assets provided for in the *BIA* (as will be discussed below), as termination and severance pay are specifically excluded under that Act.²¹ What this essentially means is that, while the government will compensate employees under the WEPP for termination and severance pay to which they are entitled, these additional amounts are not included in the priority charge for wages.

This becomes a relevant consideration when looking at how the WEPP payments are allocated when paid to the employee. In terms of the allocation of payments, amounts in respect of wages and vacation pay are allocated first. Termination and severance pay are allocated last among all payments made under the Act. To give a specific example, if the federal government pays \$3,000 on a claim to

¹⁷ *WEPPA*, s. 6 and *WEPPA Regulations*, ss. 4 and 5.

¹⁸ *Budget Implementation Act*, 2009, S.C. 2009, c. 2.

¹⁹ For instance, see the *Employment Standards Act, 2000*, S. O. 2000, c. 41.

²⁰ E. Patrick Shea, *BIA, CCAA & WEPPA A Guide to the New Bankruptcy & Insolvency Regime* (LexisNexis Canada Inc., 2009) at 256.

²¹ *BIA*, s. 81.3(9) and s. 81.4(9).

an employee, and, of that amount, \$1,000 is for termination pay and \$2,000 of which is for unpaid wages, the government will still be able to assert the \$2,000 priority charge under the *BIA*.²²

Role of the Trustee/Receiver

The trustee in bankruptcy / receiver has obligations to both employees and the Minister under WEPPA. The trustee or receiver must identify every individual who is owed eligible wages, determine the amount owed, inform each individual of the program, and inform the Minister when the trustee or receiver is discharged or completes its duties, respectively. The trustee or receiver has 45 days (or longer if circumstances beyond the trustee/receiver's control necessitate otherwise) from the date of bankruptcy or the first date on which there was a receiver to provide the following information to the Minister regarding individuals who are owed eligible wages:

- (a) the date of bankruptcy or receivership;
- (b) the name, address, telephone number, social insurance number, employee number and job title of the individual;
- (c) the dates on which wages, other than severance pay or termination pay, were earned and the basis upon which they were calculated;
- (c.1) the date on which any employment in respect of which severance pay or termination pay is owing ended;
- (d) a statement as to whether or not the individual submitted a proof of claim for wages owing under section 124 of the *Bankruptcy and Insolvency Act*; and
- (e) the names of the employer's officers, directors and owners and of the person responsible for the employer's payroll.²³

²² *WEPPA Regulations*, s. 8.

²³ *WEPPA*, s. 21.

The trustee or receiver must also provide the following information to individuals within 45 days:

- (a) the date of bankruptcy or receivership;
- (b) a statement informing the individual of their requirement under section 124 of the Bankruptcy and Insolvency Act to submit a proof of claim for wages owing;
- (c) a copy of the information and documents that they provided to the Minister with respect to the individual; and
- (d) an application form for the WEPP.²⁴

These additional tasks are quite an onerous burden for trustee/receivers, particularly when confronted with inadequate books and records. This will add considerably to the cost of a bankruptcy or a receivership, a cost which is ultimately borne by the secured creditors.

How it Works from the Creditor's Perspective

The Wage Charge

In addition to the introduction of *WEPPA*, corresponding amendments were made to the BIA. These amendments created a super-priority charge in a bankruptcy or a receivership with respect to unpaid wages (the "Wage Charge") which ranks above secured claims.

The Wage Charge has a limit of \$2,000 per employee for wages, salaries, commissions or compensation for services rendered, and up to \$1,000 for disbursements owed to travelling salespeople. The relevant period is six months prior to the initial bankruptcy event and ending on the date of the bankruptcy or six months prior to the date of the appointment of a receiver.²⁵

There has been some confusion created by this limit as the Wage Charge does not match the amount that can be claimed by employees through the WEPP. However, the WEPP amount and the Wage

²⁴ *WEPPA Regulations*, s. 16.

²⁵ *BIA*, ss. 81.3(1), (3) and 81.4(1), (3).

Charge must be regarded as distinct amounts. Essentially, the cap on any amounts actually paid to an employee under the WEPP is \$3,000. This payment are subrogated to the federal government and, in turn, the federal government will recoup amounts paid by way of the Wage Charge, which secures up to \$2,000 per employee, from the estate of the employer who is bankrupt or subject to a receivership. To assist the reader, a helpful chart distinguishing the key aspects between the WEPP amount and the Wage Charge is included at Appendix A to this paper.

As with the WEPP, the Wage Charge is not extended to the company's directors and officers or persons who did not deal with the company at arm's length.²⁶

The Extent of the Charge

The Wage Charge is created over the current assets of the employer as at the date of bankruptcy. "Current assets" is defined as cash, cash equivalents — including negotiable instruments and demand deposits — inventory or accounts receivable, or the proceeds from any dealing with those assets.²⁷ It is notable that the priority claim does not extend to equipment, real property or other assets of a bankrupt employer.

There is a slight distinction in the case of a receiver. In such cases, the Wage Charge appears to only attach to the debtor's current assets that are "in the possession or under the control" of the receiver.²⁸ In other words, if a receiver is not appointed over all of the debtor's assets, then the Wage Charge would not extend to the "excluded" assets.

Other exclusions from the Wage Charge include unpaid sellers seeking to repossess goods delivered to the debtor within 30 days of the bankruptcy²⁹ and the claims of unpaid farmers, fishermen and aquaculturists for unpaid amounts relating to products delivered to the debtor.³⁰

²⁶ *BIA*, ss. 81.3(6), (7) and 81.4(6), (7).

²⁷ *BIA*, s. 2.

²⁸ *BIA*, s. 81.4(1).

²⁹ *BIA*, s. 81.1.

Limiting the Impact of the Wage Charge

To limit the impact of the priority charge, secured creditors may consider altering their lending practices in the following ways:

the lender requires the borrower to hire an external payroll service to administer payroll. This ensures that wages are kept current and source deductions are automatically remitted;

the borrower is required to give additional security to cover the possibility of increased exposure under the priority charge;

the lender conducts more frequent spot audits of the borrower's books and records; and

the lender reduces the borrower's financing limits.

Single Creditors Can be Targeted

Another important consideration for a secured creditor is how the priority charge is paid. Often a single secured creditor may find itself bearing the brunt of the priority charge despite the presence of multiple secured creditors. Regrettably, the amendments to the BIA do not contain a process by which a secured creditor can require other creditors to share the burden of the priority charge. At best, the creditor is left with a preferred claim in the bankruptcy for any amounts paid under the charge.³¹

As preferred claims rank after secured claims, a secured lender would be well served by entering into an intercreditor agreement with other secured lenders in order to ensure that the priority charge is shared in some equitable manner. The incentive to other secured lenders is that they will have a

³⁰ BIA, s. 81.2.

³¹ BIA, s. 136(1)(d.01) and (d.02),

contractual basis to compel payment from the parties to the agreement should they be targeted in a multiple creditor situation.

Private Receivers and Enforcing Security

Secured creditors considering enforcing their security outside of a bankruptcy or a court appointed receivership proceeding should be aware that due to the broad definition of “receiver” under the BIA³², their enforcement proceedings may activate obligations under WEPPA and the priority charge.

WEPPA and the priority charge can also be activated in circumstances in which a creditor has privately appointed a receiver under its security agreement or is acting as its own receiver by taking possession or control of substantially all of the inventory, accounts receivable or other business property of a debtor pursuant to a security agreement.

Therefore, secured creditors who take steps to enforce their own security must comply with the requirements under WEPPA and the notice and reporting obligations under the BIA. This means that the secured creditor will be required to register with the Office of the Superintendent of Bankruptcy as a receiver, provide former employees with notice of their ability to make a claim to the WEPP and assist former employees with their WEPP claims.

These administrative duties are in addition to dealing with any super-priority claims against the employer’s current assets that former employees may be able to assert under WEPPA for outstanding wages and unpaid pension contributions.

In such cases, the creditor would be wise to consider retaining a qualified accounting firm to deal with the compliance aspects of the WEPPA.

Pension Priorities

In addition to the Wage Charge, the BIA was also amended to include a charge to secure unpaid pension amounts (the “Pension Charge”). The Pension Charge will apply where: (a) the debtor becomes bankrupt on or after July 7, 2008 (or the bankruptcy is the result of proposal proceedings

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BIA, s. 243(2).

commenced on or after July 7, 2008); or (b) all of part of the debtor's property comes into the possession or control of a receiver on or after July 7, 2008.³³

By way of background, pensions established in Ontario are governed by the *Pension Benefits Act*³⁴ [*PBA*]. Pensions can be divided into two broad categories: defined contribution and defined benefit. As one might expect, in defined contribution plans, the employer makes pre-determined contributions, whereas in defined benefit plans, employer contributions are generally calculated via an actuarial method. Section 4 of the *PBA* sets out general pension plan funding requirements. The employer is required to make payments within thirty days after the month for which the contributions are payable. The actual amounts funded by employers and the ratio of the employer's contribution to the employee's contribution will vary depending on the agreement.

In bankruptcy proceedings under the *BIA* prior to the amendments, employees who had amounts withdrawn by their employers from their remuneration to be put toward a pension plan nonetheless ranked below secured creditors in respect of those amounts. Despite the fact that the *PBA* establishes that money received by an employer from an employee for the purpose of adding it to the pension fund is subject to a deemed trust, courts have held that this does not constitute "trust property" for the purposes of the *BIA*, a designation which would rank the employee above a secured creditor in respect of that amount.³⁵

Although WEPPA does not directly address pension contributions, the *BIA* and the *CCAA* were concurrently amended with the establishment of WEPPA to provide protection to employees in relation to employer pension plan contributions.³⁶ The amendments to the *BIA* came into force at the same time as WEPPA in July 2008.³⁷ The result was the Pension Charge which extends over *all the assets of the employer*. This is in contrast to the Wage Charge, which only extends to current assets.

³³ *BIA*, ss. 81.5 and 81.6.

³⁴ *Pension Benefits Act*, R.S.O. 1990, C. P.8 [*PBA*].

³⁵ See, for example, *Ivaco Inc. (Re)*, [2006] O.J. No. 4152 (C.A.).

³⁶ *BIA*, ss. 81.5 and 81.6.

³⁷ *BIA*, ss. 81.5 and 81.6.

Another difference from the Wage Charge is that the Pension Charge extends to all real and personal property. Further, the Pension Charge has no monetary limit.

With regard to both bankruptcies and receiverships, the Pension Charge secures several amounts including, all amounts deducted from the employee's remuneration for payment to the fund and unpaid employer contributions to defined contribution plans.

In terms of priority, the Pension Charge ranks directly behind the Wage Charge as outlined in sections 81.3 and 81.4 in the *BIA*. In other words, the government will recover amounts paid under WEPPA through subrogated claims first before an employee will be awarded unpaid pension funds out of common assets of the bankrupt company.

Priorities in Other Insolvency Proceedings

There are two other procedures relating to insolvent entities which have not yet been canvassed: a restructuring under the *CCAA* and a proposal under the *BIA*. The idea behind both processes is to allow the insolvent entity to relieve itself from some of its obligations to creditors with the goal of emerging as a solvent, viable entity.

The WEPPA-related amendments respecting these two restructuring mechanisms were not proclaimed into force until September 2009. As they involve the corporation continuing to operate (as opposed to a distribution of the corporation's assets) the wording is slightly different, but nonetheless closely mirrors the spirit of the provisions relating to bankruptcy and receivership. In order for a court to approve a proposal under the *BIA* (or a "compromise" under the *CCAA*), the proposal or compromise must provide for payment of all the same amounts which constitute the charge under the bankruptcy and restructuring sections.³⁸ The relevant sections in both statutes require that a proposal or plan provide for payment of the following:

- (i) an amount equal to the sum of all amounts that were deducted from the employees' remuneration for payment to the fund,

³⁸ *BIA*, s. 60(1.5) and *CCAA*, s. 6(6).

(ii) if the prescribed pension plan is regulated by an Act of Parliament,

(A) an amount equal to the normal cost, within the meaning of subsection 2(1) of the *Pension Benefits Standards Regulations, 1985*, that was required to be paid by the employer to the fund, and

(B) an amount equal to the sum of all amounts that were required to be paid by the employer to the fund under a defined contribution provision, within the meaning of subsection 2(1) of the *Pension Benefits Standards Act, 1985*; and

(iii) in the case of any other prescribed pension plan,

(A) an amount equal to the amount that would be the normal cost, within the meaning of subsection 2(1) of the *Pension Benefits Standards Regulations, 1985*, that the employer would be required to pay to the fund if the prescribed plan were regulated by an Act of Parliament, and

(B) an amount equal to the sum of all amounts that would have been required to be paid by the employer to the fund under a defined contribution provision, within the meaning of subsection 2(1) of the *Pension Benefits Standards Act, 1985*, if the prescribed plan were regulated by an Act of Parliament;

The court must also be satisfied that the employer can and will make the payments as required under the compromise or proposal.

Conclusion

The introduction of WEPPA and related amendments established a new regime to give employees better protections where their employer becomes bankrupt or insolvent. As it stands, the four primary types of insolvency proceedings (bankruptcy, BIA proposal, receivership and a CCAA restructuring) all contain similar levels of protection for wage earners, particularly in respect to pension contributions. Therefore, not only are employees able to recover some of their unpaid wages, but there is an unlimited charge relating to certain pension amounts. Both elements significantly improve the situation for this class of involuntary creditors.

However, these protections have come at a cost for secured creditors. This, coupled with the current state of the economy, has definitely had an adverse impact on lending practices.

There have been very few cases so far dealing with WEPPA in the year and a half since it has been in force. As use of the program becomes more commonplace, and in the face of continuing economic difficulties in Canada and abroad, we can expect judicial interpretation of WEPPA and related amendments to increase in the coming years. It is yet too early to tell whether WEPPA will provide wage earners with adequate protection in the face of employer insolvencies, or whether the administrative burden and demotion of the rights of secured creditors will have an effect on business practices and the overall effectiveness of the program. WEPPA is set for review by Parliament five years after it was proclaimed in force;³⁹ by that time, we will have a better idea of whether it has in fact adequately balanced the competing interests at play.

³⁹

WEPPA, s. 42.

APPENDIX A

Description	Service Canada Claim under WEPPA	Claim Against the Estate under BIA
Definition of Wages	Wages includes salary, commissions, compensation for services rendered during the 6 months before the bankruptcy or receivership. WEPPA includes severance and termination pay.	Wages includes salary, commissions, compensation for services rendered during the 6 months before the bankruptcy or receivership. BIA specifically excludes severance and termination pay from the definition of compensation (see s. 81.3 (9) and s. 81.4(9) of the BIA).
Maximum Claim	Maximum is 4 weeks maximum insurable earning under the employment insurance (Approximately \$3,250).	Maximum is \$2,000 per employee (and \$1,000 for each traveling salesman's disbursements). Amount is reduced by any amounts paid by the trustee or receiver.
Security or Payment Provision	Employees make claim to Service Canada and are paid by Government of Canada.	The BIA provides that the trustee or receiver is liable for the Estate Claim to the extent of the amount realized from the disposition of current assets. BIA provides that security for Estate Claim "ranks above every other claim, right, charge or security against the person's current assets" except for claims under section 81.1 (30 day good claim) and section 81.2 (special rights of farmer, fisherman and aquaculturists)

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