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• CROSS-BORDER INSOLVENCY: CANADIAN RECOGNITION OF A FOREIGN MAIN PROCEEDING IN THE MtGOX BITCOIN EXCHANGE BANKRUPTCY •

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The prevalence of e-commerce means that many businesses are now truly international. Customers often don't give much thought to whether an e-commerce business is located down the street or on the other side of the world. When an e-commerce business falls into insolvency, the complications of having creditors in many jurisdictions can have enormous impact on stakeholders and on the administration of the insolvent company's estate.

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LexisNexis

The MtGox bitcoin exchange insolvency provides a good example of the complications caused by the bankruptcy of a large e-commerce business and the insolvency law tools available to address them.

At one time, the MtGox exchange was reported to be the largest online bitcoin exchange in the world. In February 2014, MtGox halted all bitcoin withdrawals by its customers after it was subject to what appears to have been a massive theft or disappearance of bitcoins held by it. These events caused, among other things, MtGox to become insolvent, and ultimately led to MtGox's Japanese bankruptcy proceeding. MtGox had approximately 120,000 customers in 175 countries—including Canada—who had a bitcoin or fiat currency balance in their accounts as of the date of the insolvency. The fallout of the insolvency and freezing of customer accounts included the filing of class action proceedings on behalf of customers in the U.S. and Canada.

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While the Japanese bankruptcy proceeding commenced on April 24, 2014, it was not until the statement of claim in the pending class action filed in the Ontario Superior Court of Justice was provided to the Japanese bankruptcy trustee of MtGox (the "Trustee") under the Hague Convention on August 29, 2014, that the Trustee sought recognition of the Japan bankruptcy proceeding in Canada. The Trustee sought recognition of the Japan bankruptcy proceeding in an effort to maximize recoveries to, and provide for an equitable distribution of value among, all creditors. On October 3, 2014, Justice Newbould granted a recognition order recognizing the Japanese bankruptcy proceeding as a foreign main proceeding and providing a stay of proceedings.[1]

The Conflict of Law Theory

As found by Newbould J., the conflicts of law theory, which has been embodied in jurisdictions, including Canada, who have adopted in whole or in part the United Nations Commission on International Trade Law (*UNCITRAL*) Model Law on Cross Border Insolvency, has been called *modified universalism*. Justice Newbould noted that

> Universalism is a theory that posits that the bankruptcy law to be applied should be that of the debtor's home jurisdiction, that all of the assets of the insolvent corporation, in whichever country they are situated, should be pooled together and administered by the court of the home country. Local courts in other countries would be expected, under universalism, to recognize and enforce the judgment of the home country's court. This theory of universalism has not taken hold. …
>
> The notion of modified universalism is court recognition of main proceedings in one jurisdiction and non-main proceedings in other jurisdictions, representing some compromise of state sovereignty under domestic proceedings to advance international comity and cooperation.[2]

The Requirements

Part XIII (ss. 267–284) of the *Bankruptcy and Insolvency Act* [*BIA*][3] address cross-border

insolvencies and set out the provisions with respect to obtaining a recognition order. Sections 46–51 of the *Companies' Creditors Arrangement Act* [*CCAA*][4] also govern recognition of foreign proceedings. The statutory provisions spell out the requirements for obtaining an order recognizing a foreign proceeding. There are three main requirements:

(i) establish that the proceeding is a "foreign proceeding" as defined by the *BIA* or the *CCAA*,

(ii) establish that the applicant is a "foreign representative" as defined by the *BIA* or the *CCAA*, and

(iii) establish whether the "foreign proceeding" is a "foreign main proceeding" or a "foreign non-main proceeding".

Foreign Proceeding

Pursuant to s. 270(1) of the *BIA*, the court shall make an order recognizing the foreign proceeding if (1) the proceeding is a foreign proceeding, and (2) the applicant is a foreign representative of that proceeding.

A "foreign proceeding" is defined in s. 268(1) of the *BIA* to mean "a judicial or an administrative proceeding […] in a jurisdiction outside Canada dealing with creditor's collective interests generally under any law relating to bankruptcy or insolvency in which a debtor's property and affairs are subject to control or supervision by a foreign court for the purpose of reorganization or liquidation".

In *MtGox*, there was detailed evidence before the Superior Court regarding the ties between the company and Japan,[5] the Japanese bankruptcy proceeding, and also with respect to the Japan *Bankruptcy Act*. Justice Newbould found that the Japanese bankruptcy proceeding

> is a judicial proceeding dealing with creditors' collective interests generally under the Japan Bankruptcy Act, which is a law relating to bankruptcy and insolvency, in which MtGox's property is subject to supervision by the Tokyo District Court, Twentieth Civil Division. As such, the Japan bankruptcy proceeding is a foreign proceeding pursuant to section 268(1) of the BIA.[6]

Foreign Representative

A "foreign representative" is defined in s. 268(1) of the *BIA* to mean

> a person or body, including one appointed on an interim basis, who is authorized, in a foreign proceeding in respect of a debtor, to
>
> (a) administer the debtor's property or affairs for the purpose of reorganization or liquidation; or
>
> (b) act as a representative in respect of the foreign proceeding.

In MtGox, Newbould J. found that the Trustee was a "foreign representative":

> The Trustee has authority, pursuant to the Japan Bankruptcy Act and the bankruptcy order made by the Tokyo District Court in the Japan bankruptcy proceeding, to administer MtGox's property and affairs for the purpose of liquidation and to act as a foreign representative. Thus the Trustee is a foreign representative pursuant to section 268(1) of the BIA.[7]

Foreign Main Proceeding or Foreign Non-main Proceeding

The significance of whether a foreign proceeding is a "foreign main proceeding" or a "foreign non-main proceeding" is that there is an automatic stay provided in s. 271(1) of the *BIA* if the proceeding is a "foreign main proceeding", and, if it is a "foreign non-main proceeding", then an application must be made for a stay.

Section 268(1) defines a foreign main proceeding as a proceeding in a jurisdiction where the debtor has its centre of main interest (referred to in the caselaw as "COMI"). There is a rebuttable presumption that a debtor's COMI is in jurisdiction where its registered office is located.

In *MtGox*, Newbould J. found that the Japanese bankruptcy proceeding was a foreign main proceeding. In his reasons he notes the following with respect to COMI:

[20] A foreign main proceeding is defined in section 268(1) as a foreign proceeding in a jurisdiction where the debtor company has the centre of its main interests (COMI). Section 268(2) provides that in the absence of proof to the contrary, a debtor company's registered office is deemed to be the centre of its main interests.

[21] In considering whether the registered office presumption has been rebutted a court should consider the following factors in determining COMI (i) the location is readily ascertainable by creditors (ii) the location is one in which the debtor's principal assets and operations are found and (iii) the location is where the management of the debtor takes place. See *Lightsquared LLP, Re* (2012), 92 C.B.R. (5th) 321.

[22] The Trustee relies on the following facts in support of his position that the COMI of MtGox is in Japan and not in Canada.

> (1) MtGox has no offices in Canada, there are no Canadian subsidiaries and no assets located in Canada.
>
> (2) MtGox is and has always been organized under the laws of Japan.
>
> (3) MtGox's registered office and corporate headquarters are, and have always been, located in Japan, and its books and records are located at its head office in Japan.
>
> (4) The Debtor's sole director and representative director, Mr. Karpeles, resides, and at all relevant times has resided, in Japan.
>
> (5) Most of the MtGox's bank accounts are located in Japan, including the primary account for operating its business.
>
> (6) MtGox's parent company, Tibanne, provided operational and administrative services to it, including the provision of its primary workforce, in Japan.
>
> (7) MtGox's Website clearly disclosed to customers and other third parties that it is a Japanese corporation that is located in Japan.
>
> (8) Upon the filing of the Japan Petition, MtGox commenced an investigation in Japan with regard to the circumstances that led to the Japan civil rehabilitation, which investigation was subject to the oversight of the Tokyo Court.

[23] Taking into account this evidence, I am satisfied that the COMI of MtGox is its registered head office in Japan and that the Japan bankruptcy proceeding is a foreign main proceeding.

Practical Considerations

The following is a list of tips and practical considerations in bringing an application for a recognition order.

The Stay

A foreign proceeding can be found to be a foreign main proceeding or a foreign non-main proceeding. If the foreign proceeding is recognized as a main proceeding, there is an automatic stay provided in s. 271(1) against any action concerning the debtor's property, debts, liabilities, or obligations. If the foreign proceeding is recognized as a non-main proceeding, there is no such automatic stay, and it is necessary for an application to be made to obtain such relief. In addition to the stay, s. 271(1) also mandates that the recognition order must provide for a prohibition on dispositions of property by the debtor outside the ordinary course of business.

Model Order

Model forms of an Initial Recognition Order and Supplementary Order are available on the Ontario courts website.[8] Like with other model orders, the model order should be tailored to the circumstances of the proceeding, and a blackline of your proposed form of order as against the model order should be made available to the court. It is noteworthy that a number of provisions that are mandated by the *BIA* or the *CCAA*, so drafters should consult the applicable statute before deleting provisions that restrict dealing with assets or required notice.

Other Relief

Depending on the circumstances, the foreign representative may wish to seek other relief to facilitate the administration of the estate or securing of assets at the hearing of the application for the recognition order. The types of other relief that may be sought include appointment of a receiver over assets located in the jurisdiction,

orders to interview people with knowledge of the affairs or assets of the debtor, and the appointment of an information officer.

Certified Copy of the Foreign Bankruptcy Order

The application must be accompanied by a certified copy of (1) the instrument that commenced the foreign proceeding, and (2) the instrument that authorized the foreign representative to act. Obtaining a certified copy of a foreign order or instrument may take some time, and so this should be requested as soon as practicable. In addition, a translation of the foreign order or instrument may also be required.

Recognition Orders in Other Jurisdictions

The application materials are required to include a statement identifying all foreign proceedings in respect of the debtor that are known to the foreign representative.[9]

Newspaper Notice

Section 276(b) of the *BIA* mandates that a notice be published "once a week for two consecutive weeks […] in one or more newspapers in Canada specified by the court". The content of the notice is prescribed by s. 138 of *Bankruptcy and Insolvency General Rules*.[10] Section 53 of the *CCAA* also sets out a newspaper notice requirement.

Ongoing Obligations

After a recognition order is made, the foreign representative who applied for the order is required to keep the court informed of any substantial change in the status of the recognized foreign proceeding.

Summary

The foreign recognition order provisions of the *BIA* and the *CCAA* have simplified the process for obtaining recognition of foreign insolvency proceedings in Canada. With the prevalence of cross-border insolvencies, recognition orders can be a useful tool to (1) assist efforts to maximize recoveries to all creditors worldwide, and (2) avoid problems caused by piecemeal litigation and claims in multiple jurisdictions.

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1 *MtGox Co., Ltd (Re)*, [2014] O.J. No. 4719, 2014 ONSC 5811, 122 O.R. (3d) 465 (Commercial List) [*MtGox*].
2 *Ibid*., paras. 10–11.
3 *BIA*, R.S.C., 1985, c. B-3.
4 *CCAA*, R.S.C. 1985, c. C-36.
5 For example, as the affidavit of Japanese trustee in bankruptcy explained:
   (i) MtGox Co., Ltd. ("MtGox") was organized as a corporation under the laws of Japan on August 9, 2011.
   (ii) MtGox's corporate headquarters were always in Tokyo—subleased from a Japanese corporation ("Tibanne") which was the majority shareholder of MtGox.
   (iii) the sole director of MtGox was ("and ha[d] always been") a resident of Japan. There was never "a board of directors" beyond that individual director.
   (iv) MtGox's financial statements were prepared by "a Japan-based accounting firm."
   (v) MtGox's employees were supplied by Tibanne and "all of […those] employees that …ever worked for [MtGox] performed their work in Japan."
   (vi) "Prior to the shutdown of the MtGox Exchange in February 2014, the Website clearly communicated to customers and other parties that [MtGox] is a Japanese company that is located in Japan."
   (vii) "Similarly, [MtGox's] Website's "Privacy Policy" page … also noted the Tokyo address of [MtGox's] Head Office along with [MtGox's] Tokyo phone number.
   (viii) "In addition, the Website's "About Us" page … contained a link to [MtGox's] official registration at the Tokyo Chamber of Commerce."

Justice Newbould cited these and other factors in para. 22 of his decision, quoted *infra*, in support of his conclusion that the *MtGox* proceeding was a foreign main proceeding.

6 *MtGox*, *supra* note 1, para. 15.

7 *Ibid.*, para. 17.

8 <http://www.ontariocourts.ca/scj/practice/practice-directions/toronto/>.

9 *BIA*, *supra* note 3, s. 269(1)(*c*).

10 C.R.C., c. 368.

• CASE COMMENT: *RE NORTEL NETWORKS CORP.* AND THE APPLICABILITY OF THE *INTEREST STOPS* RULE TO *CCAA* PROCEEDINGS •

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Introduction

Nortel Networks Corporation ("NNC") and other Canadian debtors were granted protection under the *Companies' Creditors Arrangement Act* [*CCAA*][1] on January 14, 2009.[2] On that date, Nortel Networks Inc. ("NNI") and other U.S. debtors filed petitions under Chapter 11 of the *U.S. Bankruptcy Code*.[3] As the proceedings evolved and various asset sales were completed with joint court approval, it became apparent that Nortel would not restructure as a going concern. In other words, the case had effectively become a "liquidating" *CCAA* proceeding. A joint trial was directed by the Ontario Superior Court of Justice and the United States Bankruptcy Court for the District of Delaware to determine how the sale proceeds of approximately US $7.3 billion are to be allocated (the "Allocation Trial").

In June 2014, the Superior Court of Justice and the U.S. Bankruptcy Court, at the time jointly hearing the Allocation Trial, directed that the issue of the entitlement of certain bondholders to receive interest accruing since the commencement of Nortel's insolvency proceedings be argued. The hearing in the U.S. Bankruptcy Court was adjourned following an apparent settlement between the U.S. Debtors and the U.S. Unsecured Creditors Committee. The hearing before the Honourable Justice Newbould of the Superior Court of Justice proceeded on July 25, 2014, and Newbould J. rendered his decision on August 19, 2014.[4]

In this case comment, the authors provide a summary of the decision and discuss Newbould J.'s analysis of the applicability of the *interest stops* rule to proceedings commenced under the *CCAA*. It is important to note that just prior to the finalization of this case comment, the Court of Appeal for Ontario granted leave to appeal from Newbould J.'s decision on the applicability of the interest stops rule. It therefore appears that Newbould J.'s ruling will not be the last word in the case on a very important issue.

Facts

Beginning in 1996, U.S. and Canadian Nortel corporations issued unsecured *pari passu* bonds under three different bond indentures. Some of these bonds were issued by a U.S. Nortel corporation in several tranches and were jointly and severally guaranteed by NNC and NNI. Under claims procedures in the Canadian and U.S. insolvency proceedings, bondholders made claims for principal and pre-filing interest against the Canadian and U.S. estates amounting to US$4.092 billion. The bondholders also claimed entitlement to post-filing interest amounting to US$1.6 billion as of December 31, 2013.

Issues

In the joint direction made by the Ontario and U.S. courts during the Allocation Trial, the following issues were ordered to be argued:

- whether the holders of the bond claims were legally entitled to claim or receive any amounts under the relevant indentures above and beyond the outstanding principal debt and pre-petition interest; and
- if so, what additional amounts such holders were entitled to claim and receive.

Positions of Key Stakeholders

The Monitor and Canadian Debtors argued that post-filing interest on the bonds was not legally payable in a "liquidating" *CCAA* proceeding because of the operation of the common law interest stops rule. In contrast, the Ad Hoc Group of Bondholders took the position that there was no interest stops rule in *CCAA* proceedings and that post-filing interest on the bonds was one of the matters to be negotiated in a *CCAA* plan of reorganization. Further, they argued that the court could not order a distribution under the *CCAA* of Nortel's sale proceeds that does not recognize the full amount of the bondholders' claims, including post-filing interest, except by sanctioning a negotiated *CCAA* plan approved by the required majority of creditors and sanctioned by the court.

The Decision

Justice Newbould accepted the position of the Monitor and Canadian Debtors and ruled that post-filing interest was not legally payable on the bonds in the case before him.

His Honour commenced his analysis by referencing the fundamental principle of insolvency law that all debts are to be paid *pari passu* and all unsecured creditors are to receive equal treatment. This principle has led to the development of the interest stops rule, which arose at common law to effectively freeze all unsecured claims to the debtor's estate as at the date of bankruptcy.[5] Justice Newbould noted that the interest stops rule had been applied in bankruptcy and winding-up cases where the relevant legislation did not specifically provide for its application but also did not preclude it.[6] He extended the reasoning in these cases to the *CCAA,* observing that the absence of an express interest stops rule in the *CCAA* is no reason not to apply it to a *CCAA* case and concluding that the rule should be applied to the *Nortel* case—in his view, a "liquidating" *CCAA* proceeding[7] analogous to a bankruptcy if no plan is filed and implemented.

Justice Newbould went further by observing, it appears by way of *obiter dicta,* that there is no need for the *CCAA* case to be liquidating in nature in order for the interest stops rule to apply to the proceeding.[8]

Justice Newbould arrived at his conclusions largely on the basis of the importance of both (1) harmonizing the results effected under the *CCAA* and *Bankruptcy and Insolvency Act* [*BIA*][9] and (2) maintaining the *status quo* among unsecured creditors during the course of the *CCAA* proceedings. In addition, he distinguished two appellate level cases relied on by the bondholders. Before embarking on explaining his reasoning, Newbould J. expressed the following view:

> There is no controlling authority in Canada in a case such as this in which there is a contested claim being made by bondholders for post-filing interest against an insolvent estate under the CCAA, let alone under a liquidating CCAA process, or in which the other creditors are mainly pensioners with no contractual right to post-filing interest. Accordingly, it is necessary to deal with first principles and with various cases raised by the parties.[10]

Justice Newbould relied principally on the Supreme Court of Canada's decision in *Century Services Inc. v. Canada (Attorney General)* [*Century Services*][11] to stress the importance of preserving the *status quo* in a restructuring case and harmonizing the two insolvency statutes. In that case, the Supreme Court reaffirmed that the purpose of a *CCAA* stay of proceedings was to preserve the *status quo.* Justice Newbould

referred to the Supreme Court's statements that the *BIA* and *CCAA* create a comprehensive insolvency regime and that the courts favour interpretations of the statutes that give creditors analogous entitlements under the *CCAA* and *BIA*. Based on the foregoing, he concluded that there is no reason not to apply the interest stops rule in a liquidating *CCAA* proceeding.

Justice Newbould's observations in para. 33 of his reasons are helpful in understanding how he reached his conclusions:

> Thus, it is a fair comment taken the direction of the Supreme Court in *Century Services* and *Indalex* regarding the aims of insolvency law in Canada to say that if the common law principle of the interest stops rule was applicable to proceedings under the BIA and *Winding-Up Act* before legislative amendments to those status were made (or if the comments of Blair J. in *Confederation Life* are accepted that the BIA still might be read to prevent its application but does not trump the application of the rule), there is no reason not to apply the interest stops rule in liquidating CCAA proceedings. I accept this and note that there is no provision in the CCAA that would not permit the application of the rule.[12]

From a policy perspective, Newbould J. agreed with the position of the Canadian Creditors' Committee that it would be unfair to allow some creditors' claims to grow disproportionately to others during the *CCAA* stay period—this would not maintain the *status quo* and would provide undesirable incentives to certain creditors to initiate bankruptcy proceedings, thus threatening the *CCAA*'s objectives.[13]

As indicated above, Newbould J. also stated his view that the interest stops rule applies to *CCAA* proceedings other than liquidating cases, noting, however, that post-filing interest could be included in a plan. In his opinion, the objective of preventing a stay from favouring one group of unsecured creditors to the detriment of another group applies equally to a *CCAA* proceeding that is not liquidating.[14] It appears that these observations were *obiter dicta,* and it will be interesting to see how other courts treat them.

Notably, Newbould J. distinguished two important decisions in concluding that post-filing interest was not legally payable on the bonds. The first, *Re Stelco Inc.* [*Stelco*],[15] involved a successful restructuring of the debtor company by a plan of compromise or arrangement that did not provide for the payment of post-filing interest. In its reasons in *Stelco*, the Ontario Court of Appeal stated that there was no persuasive authority supporting an interest stops rule in a *CCAA* proceeding.[16] Justice Newbould distinguished the case on the basis that it did not involve a claim for post-filing interest against the debtor, but a dispute between two classes of debenture holders. The pre-filing indenture in *Stelco* provided that all senior debenture holders would be entitled to receive payment in full of principal and interest before the junior debenture holders would be entitled to receive a distribution or payment of any kind. The *CCAA* plan sanctioned by the court preserved all rights between debenture holders. After the plan had been sanctioned, the junior debenture holders challenged the senior debenture holders' right to receive the subordinated payments towards their interest. The Court of Appeal upheld the trial judge's decision that the interest stops rule did not prevent the continuation of interest payments to the senior debenture holders by the junior debenture holders according to the terms of the inter-creditor arrangement.

The second case, *Re Inter Canadian (1991) Inc. (Trustee of) Canada 3000 Inc.* [*NAV Canada*],[17] involved a contest between the airport authorities and the owners/lessors of aircraft over liability for outstanding payments owed by the airline for using airport facilities, and whether certain aircraft leased to the airline could be seized to cover the payments. The airline, Canada 3000, filed for *CCAA* protection, and the Monitor filed an assignment in bankruptcy on its behalf three days later. The motions judge held that the owners/lessors were not liable for

the outstanding payments owed by the airline but the aircraft could be seized. Further, the motions judge concluded that the airport authorities were entitled to detain the aircraft until all amounts, including interest, were paid in full—in his view, interest continued to accrue and be payable after bankruptcy. The Court of Appeal did not rule on the issue, but the Supreme Court briefly dealt with the interest question, and Justice Binnie observed that a *CCAA* filing did not stop the accrual of interest.[18] In his reasons, Newbould J. noted that Binnie J.'s comments "should not be taken as a blanket statement that interest always accrues in a *CCAA* proceeding",[19] liquidating or non-liquidating, as the Supreme Court did not analyze the interest stops rule by considering the applicable common law and *CCAA* provisions; the statement was in Newbould J.'s words "simply conclusory" and "it may be fair that the statement of Binnie J. was *per incuriam*".[20] Justice Newbould also distinguished the circumstances of the *NAV Canada* case, noting that the *Nortel* case involved several years of compound post-filing interest exceeding $1.6 billion.[21]

Justice Newbould then turned to the bondholders' argument that the court did not have the authority to effect a distribution of a debtor's assets in a *CCAA* proceeding absent a plan of arrangement or compromise negotiated by the debtor with its creditors. The bondholders contended that since a plan can include the payment of post-filing interest, the court could not conclude that the bondholders had no right to it and did not have the jurisdiction to compromise a creditors' claim except in the context of sanctioning a creditor-approved plan.

Before analyzing this argument by the bondholders, Newbould J. made the following interesting observations on the bondholders' assertion that "in earnest" negotiation on a plan could not meaningfully occur until a decision is made in the Allocation Trial:

> One may ask what is left over in this case to negotiate. The assets have long been sold and what is left is to determine the claims against the Canadian estate and, once the amount of the assets in the Canadian estate are known, distribute the assets on a *pari passu* basis. This is not a case in which equity is exchanged for debt in a reorganization of a business such as *Stelco*.
>
> However, even if there were things to negotiate, they would involve creditors compromising some right, and bargaining against those rights. What those rights are need to be determined, and often are in CCAA proceedings.[22]

Justice Newbould noted that a compensation claims procedure order covering claims by bondholders had been made on July 30, 2009, without the bondholders' objecting. The order provided for a claim to be proven for the purposes of voting and distribution under a plan. A subsequent claims resolution order dated September 16, 2010, provided for a proven claim to be for all purposes, including voting and distribution under a plan. Justice Newbould reasoned that the determination of the bondholders' claims for post-filing interest was part of the court-approved claims resolution process for establishing whether the claims were finally proven. He framed the issue as centring on whether the bondholders had a right to post-filing interest, rather than a process in which the court was being asked to compromise the claim for post-filing interest.[23]

In *obiter*, after noting that the *CCAA* is silent on how money is to be distributed to creditors, does not expressly provide for a liquidating case, and contains no requirement that distributions be made under a plan, Newbould J. added that he was "not persuaded that it would not be possible for a court to make an order distributing the proceeds of the Nortel sale without a plan of arrangement or compromise".[24] In support of this, he cited *CCAA* cases where interim and final distributions were made to secured creditors without a plan of arrangement,[25] based, he observed, on the court's equitable jurisdiction in

CCAA cases to make any order it considers just in the circumstances. This jurisdiction was effectively codified in s. 11(1) of the current *CCAA,* added in *CCAA* amendments taking effect after the *Nortel* insolvency proceedings commenced. Interestingly, no case was cited involving a distribution under the *CCAA* to unsecured creditors, such as the bondholders, without a plan being approved by the court.

Statutory Provisions Related to the Interest Stops Rule

The *Nortel* interest stops decision contains little in the way of statutory interpretation—understandably so—since, unlike the *BIA,* the *CCAA* contains no provisions referring to interest on claims. It is nevertheless useful to review the *CCAA* and *BIA* provisions relevant to post-filing interest claims on unsecured debt.

Since Nortel applied for *CCAA* protection in early 2009, its proceedings, including the Allocation Trial, are governed by the *CCAA* as it existed prior to the 2007 amendments that came into force in September 2009.[26] The pre-amendment version of the *CCAA* defined a "claim" in s. 12(1) as "any indebtedness, liability or obligation of any kind that, if unsecured, would be a debt provable in bankruptcy within the meaning of the" *BIA.* The previous version of the *CCAA* applicable to the *Nortel* case also contained the following provision:

> **Definition of "claim"**
>
> 12. (2) For the purposes of this Act, the amount represented by a claim of any secured or unsecured creditor shall be determined as follows:
>
> (*a*) the amount of an unsecured claim shall be the amount ...
>
> (iii) in the case of any other company, proof of which might be made under the *Bankruptcy and Insolvency Act*, but if the amount so provable is not admitted by the company, the amount shall be determined by the court on summary application by the company or by the creditor;

In turn, the *BIA* defines claims provable in bankruptcy in the following way:

> *Claims provable*
>
> 121. (1) All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.

The following sections of the *BIA* specifically refer to interest on unsecured claims:

> *Debts payable at a future time*
>
> 121. (3) A creditor may prove a debt not payable at the date of the bankruptcy and may receive dividends equally with the other creditors, deducting only thereout a rebate of interest at the rate of five per cent per annum computed from the declaration of a dividend to the time when the debt would have become payable according to the terms on which it was contracted.
>
> *Interest*
>
> 122. (2) If interest on any debt or sum certain is provable under this Act but the rate of interest has not been agreed on, the creditor may prove interest at a rate not exceeding five per cent per annum *to the date of the bankruptcy* from the time the debt or sum was payable, if evidenced by a written document, or, if not so evidenced, from the time notice has been given the debtor of the interest claimed [emphasis added].
>
> *Interest from date of bankruptcy*
>
> 143. Where there is a surplus after payment of the claims as provided in sections 136 to 142, it shall be applied in payment of interest *from the date of the bankruptcy* at the rate of five per cent per annum on all claims proved in the bankruptcy and according to their priority [emphasis added].
>
> *Right of bankrupt to surplus*
>
> 144. The bankrupt, or the legal personal representative or heirs of a deceased bankrupt, is entitled to any surplus remaining after payment in full of the bankrupt's creditors with interest as provided by this Act and of the costs, charges and expenses of the bankruptcy proceedings.

Based on the interpretation of these provisions and the application of common law principles in the jurisprudence, it is settled law that the

interest stops rule applies in the context of a *BIA* proceeding and similarly applies to winding-up proceedings under the *Winding-up and Restructuring Act*.[27]

The *BIA* does not have an express interest stops rule, though ss. 122(2) and 143 imply its existence in a bankruptcy case by providing, respectively, for the payment of interest on unsecured claims only to the date of bankruptcy where interest is provable but not agreed upon, and only from the date of bankruptcy where there is a surplus after payment of such claims.[28] In the latter case, the rate specified is 5 per cent per annum, which appears to override contractual rates, consistent with *pari passu* principles.

Justice Newbould's decision in *Nortel* is consistent with the implied recognition of the interest stops rule in ss. 122(2) and 143, especially in the context of a liquidating *CCAA* case. It is intriguing to consider whether by reason of the provisions of former s. 12(1) of the *CCAA*, set out above, which are applicable to the *Nortel* case, a credible argument may be made that ss. 122(2) and 143 of the *BIA* may have been effectively incorporated into the pre-amendment *CCAA* for the purposes of proving valid claims. A major impediment to the success of this argument is the following statement of the Ontario Court of Appeal in *Stelco*:

> In our view, the definition of claim in the *CCAA* is intended to set a date in order to crystallize a point in time at which claims against the company can be fixed for voting purposes in order that the estate may be administered. It has nothing to do with the amount of payments to creditors.[29]

This statement should be considered, however, in light of both the opening paragraph of s. 12(2) of the pre-amendment *CCAA,* set out above, and the provisions of s. 12(3) (now s. 20(2)). The latter section permits the debtor company to "admit the amount of a claim for voting purposes under reserve of the right to contest liability on the claim *for other purposes* [emphasis added]".

CCAA Amendments since Nortel's Insolvency Proceedings Commenced

The *CCAA* amendments that came into force in 2009 removed former s. 12(1) and introduced provisions that closely parallel the language of s. 121 of the *BIA*. Section 19(1) of the *CCAA* now reads:

> *Claims that may be dealt with by a compromise or arrangement*
>
> 19. (1) Subject to subsection (2), the only claims that may be dealt with by a compromise or arrangement in respect of a debtor company are
>
> (*a*) claims that relate to debts or liabilities, present or future, to which the company is subject on the earlier of
>
> (i) the day on which proceedings commenced under this Act, and
>
> (ii) if the company filed a notice of intention under section 50.4 of the Bankruptcy and Insolvency Act or commenced proceedings under this Act with the consent of inspectors referred to in section 116 of the Bankruptcy and Insolvency Act, the date of the initial bankruptcy event within the meaning of section 2 of that Act; and
>
> (*b*) claims that relate to debts or liabilities, present or future, to which the company may become subject before the compromise or arrangement is sanctioned by reason of any obligation incurred by the company before the earlier of the days referred to in subparagraphs (a)(i) and (ii).

The equivalent of s. 12(2) of the former *CCAA* has been re-enacted in the amended *CCAA* as s. 20(1).

An open question is whether there remains any argument along the lines of that discussed above in the context of the pre-amendment *CCAA* that under the amended *CCAA*, ss. 122(2) and 143 of the *BIA* have been effectively incorporated into the *CCAA*. The absence of an equivalent section to the previous s. 12(1) would appear to weaken

the argument for the purposes of the amended *CCAA*, but the retention of the former s. 12(2)(*a*)(*iii*) as s. 20(1)(*a*)(*iii*) seems to keep the argument, such as it is, alive.

Would the *Nortel* post-filing interest decision have been decided differently under the current *CCAA*? The desirability of harmonizing insolvency legislation may loom large in how this question is resolved if it ever comes before a court. As set out in Newbould J.'s reasons, the Supreme Court of Canada has emphasized that Parliament intended the *CCAA* and *BIA* to form a part of Canada's integrated insolvency regime and that interpretations of the two statutes that would give creditors incentives to favour one over the other should be avoided.[30] Further, the Supreme Court has stated that courts should favour interpretations of the *CCAA* that would provide creditors with similar entitlements to what they would receive under the *BIA*.[31]

In view of the approach taken by the Supreme Court in *Century Services*, it seems more likely that the issue of whether the interest stops rule applies under the amended *CCAA* will be decided on the basis of public policy and equitable principles rather than on strict statutory interpretation.

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1 *CCAA*, R.S.C. 1985, c. C-36, as amended.
2 *Nortel Networks Corp. (Re)*, [2009] O.J. No. 154, 50 C.B.R. (5th) 77 (Ont. S.C.J.).
3 *Bankruptcy Reform Act of 1978*, 11 U.S.C., as amended.
4 *Re Nortel Networks Corp.*, [2014] O.J. No. 3843, 2014 ONSC 4777.
5 *Canada (Attorney General) v. Confederation Life Insurance Co.*, [2001] O.J. No. 2610, [2001] O.T.C. 486 (Ont. S.C.J.) [*Confederation Life*].
6 *Supra* note 4, para. 15.
7 *Ibid.*, paras. 21, 23.
8 *Ibid.*, para. 35.
9 *BIA*, R.S.C. 1985, c. B-3, as amended.
10 *Supra* note 4, para. 24.
11 *Century Services*, [2010] S.C.J. No. 60, 2010 SCC 60.
12 *Supra* note 4, para. 33.
13 *Ibid.*, para. 34.
14 *Ibid.*, para. 35.
15 *Stelco*, [2007] O.J. No. 2533, 2007 ONCA 483.
16 *Ibid.*, para. 67.
17 *NAV Canada*, [2006] S.C.J. No. 24, 2006 SCC 24.
18 *Ibid.*, para. 96.
19 *Supra* note 4, para. 47.
20 *Ibid.*, para. 46.
21 *Ibid.*, para. 47.
22 *Ibid.*, paras. 49–50.
23 *Ibid.*, para. 51.
24 *Ibid.*, para. 61.
25 See *Re Timminco Limited*, [2014] O.J. No. 3270, 2014 ONSC 3393, and *Re AbitibiBowater inc.*, [2009] Q.J. No. 19125, 2009 QCCS 6461.
26 *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, 2005,* S.C. 2007, c. 36.
27 R.S.C. 1985, c. W-11, s. 71(1). See also *Shoppers Trust Co. (Liquidator of) v. Shoppers Trust Co.*, [2005] O.J. No. 1081, 74 O.R. (3d) 652 (Ont. C.A.); *Re Indalex (2009),* [2009] O.J. No. 3165, 55 C.B.R. (5th) 64 (Ont. S.C.); and *Confederation Life*, *supra* note 5.
28 As to s. 143 implying the existence of the interest stops rule in bankruptcies, this is confirmed in *Abacus Cities Ltd. (Trustee of) v. AMIC Mortgage Investment Corp.*, [1992] A.J. No. 227, 89 D.L.R. (4th) 84 (Alta. C.A.) and *McAsphalt Industries Ltd. v. Six Paws Investments Ltd.*, [1995] O.J. No. 2450, 85 O.A.C. 155 (Ont. C.A.).
29 *Supra* note 15, para 70.
30 *Supra* note 4.
31 *Sun Indalex Finance, LLC v. United Steelworkers*, [2013] S.C.J. No. 6, 2013 SCC 6, para. 51.