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Insolvency Institute of Canada (Articles)

— Director Removal under the CCAA — Marie Bruchet[FN1]

This article examines proposed amendments to the Companies' Creditors Arrangement Act (*the* "CCAA") *which would provide courts with an express power to remove directors during restructuring proceedings. It claims that the proposed director removal scheme has serious flaws and should not be adopted as part of Canadian insolvency law. The objectives of the* CCAA *are better served by the existing Canadian statutory framework.*

L'auteure examine ici les modifications proposées à la Loi sur les arrangements avec les créanciers des compagnies (la « LACC ») en vue de permettre expressément aux tribunaux de destituer des administrateurs pendant la restructuration d'une société. Elle allègue que le mécanisme de destitution d'administrateurs, tel qu'il est proposé, présente de graves lacunes et ne devrait pas être adopté dans le cadre du droit canadien sur l'insolvabilité. Selon l'auteure, le cadre législatif canadien en place permet de mieux servir les objectifs prévus da la LACC.

1. — Introduction

The success of a restructuring proceeding under the *Companies' Creditors Arrangement Act*[FN2] (the "*CCAA*") is highly dependant on a reasonable balance between the freedom of management to make governance decisions and the protection of corporate stakeholders. While not yet proclaimed into force, *Chapter 47 of the Statutes of Canada* ("*Statute c. 47*")[FN3] proposes to amend, among other things, section **11.5** of the *CCAA*. The proposed section **11.5** of the *CCAA* would provide courts with an express power to remove directors during restructuring proceedings.[FN4] Although this amendment is intended to provide a remedy that efficiently protects stakeholder interests, its potential harmful consequences have been largely overlooked.

This article argues that *Statute c. 47*'s director removal scheme has serious flaws and should not be adopted as part of Canadian insolvency law. Part 1 provides an overview of the current Canadian law in relation to director removal under the *CCAA*. Part 2 describes the recent *Statute c. 47* amendment. As an alternative to *Statute c. 47*, Part 3 describes the United Kingdom's director disqualification regime. Part 4 explains four major problems in *Statute c. 47*'s director removal scheme and provides recommendations for improvement. Finally, Part 5 proposes that there are existing mechanisms within the *CCAA* framework that make the proclamation of an express provision for director removal in the *CCAA* unnecessary.

2. — Current Canadian Law

(a) — CCAA

The *CCAA* is a short statute with a simple framework. To facilitate restructuring within the few guidelines provided, Canadian courts have adopted a liberal standard of interpretation.[FN5] Courts have relied on their broad discretion under section 11 or, in the alternative, inherent jurisdiction to "fill in gaps" and "put flesh on the bones" of the *CCAA*.[FN6]

Despite the court's willingness to exercise broad judicial intervention in *CCAA* proceedings, judges have been reluctant to second-guess corporate governance decisions made by a board of directors.[FN7] In *People's Department Stores Ltd. (1992) Inc., Re*, the Supreme Court of Canada stated that "[c]ourts are ill-suited and should be reluctant to second-guess the application of business expertise to the considerations that are involved in corporate decision making."[FN8] Furthermore, in *Brant Investments Ltd. v. KeepRite Inc.*, the Ontario Court of Appeal accepted the statement of Justice Anderson who at trial said that "[b]usiness decisions, honestly made, should not be subjected to microscopic examination. There should be no interference simply because a decision is unpopular with the minority."[FN9]

Until recently, the courts had not addressed the issue of whether a corporation's governance includes decisions relating to the composition of its board of directors. In addition, limited judicial attention has been given to the specific issue of whether the court has jurisdiction in *CCAA* proceedings to remove directors of a restructuring corporation. The restructuring of Stelco Incorporated ("Stelco") provided the first opportunity for the courts to address these matters.[FN10]

(b) — The Stelco Directors Case

On February 25, 2005, Justice Farley of the Ontario Superior Court of Justice responded to an application by Stelco's employee stakeholders for an order removing two recently appointed directors from Stelco's Board of Directors (the "Board").[FN11] The employees argued that the new directors' association with two companies, which had acquired approximately 20% of Stelco's common shares during the *CCAA* proceedings, was destabilizing to the restructuring process. Furthermore, since the new directors' appointment had been initiated by a group of shareholders who represented more than 40% of Stelco's outstanding common shares, the employees were concerned that the new directors might favour the interests of these shareholders and not have the best interests of the corporation in mind.[FN12] Justice Farley agreed to rescind the directors' appointment, relying on his "inherent jurisdiction and the discretion given to the Court pursuant to the *CCAA*."[FN13]

The Ontario Court of Appeal reversed the decision. First, Justice Blair, for a unanimous Court of Appeal, held that the lower court should not have relied on inherent jurisdiction to remove the new directors because the court's use of inherent jurisdiction is limited to procedural matters involving the court's process. Second, Justice Blair held that the court's discretion under section 11 of the *CCAA* does not include the power to remove directors because such a remedy would assume, rather than supervise, the company's restructuring efforts. Furthermore, since the power to elect, appoint and remove directors is explicitly conferred in the *Canada Business Corporations Act*[FN14] (the "*CBCA*") and its provincial equivalents, Justice Blair held that section 11's broad and undefined scope should not be extended to override this clear statutory language. Third, the Court rejected Justice Farley's view that the decision to appoint new directors should not be deferred to the Board's business judgment since it was a "quasi-constitutional aspect of the corporation." Justice Blair explained that the appointment of the new directors was a corporate governance decision relating directly to the "affairs" of the corporation as defined in section 1 of the *CBCA*.[FN15]

Finally, although not at issue in the case, Justice Blair recognized that, while section 11 of the *CCAA* alone does not provide authority for the court to remove directors, the oppression remedy provisions of the *CBCA* could be imported into the court's section 11 discretion through section 20 of the *CCAA* to allow for court removal of directors. However, this remedy would require "more than some risk of anticipated misconduct"[FN16] and was not available on the facts.

Stelco is awaiting leave to appeal to the Supreme Court of Canada.[FN17] It remains the only decision to date on the authority of the court under the *CCAA* to remove directors of a debtor corporation.[FN18] Nevertheless, it has important implications for the direction of Canadian jurisprudence in the context of corporate reorganizations and governance. The limitation of inherent jurisdiction and section 11 discretion supports a policy shift to a more rule-based approach that leaves less discretion in the hands of judges.[FN19] It confirms the reluctance of the courts to second-guess corporate governance decisions made by a board of directors. Furthermore, it suggests that the courts are less willing to use the *CCAA* to settle disputes between parties other than the debtor corporation.[FN20]

3. — The Chapter 47 Amendment

Bill C-55 was introduced to the House of Commons on June 3, 2005 and became *Statute c. 47* on November 25, 2005, after receiving Royal Assent.[FN21] While not yet proclaimed into force, *Statute c. 47* proposes, among other things, a new section **11.5** of the *CCAA* that will give the court express statutory authority to remove directors of a debtor corporation during restructuring proceedings. Under this proposed section **11.5**, where the court finds a director is "unreasonably impairing" or is "likely to unreasonably impair" the possibility of a viable reorganization, or a director is "acting" or is "likely to act" inappropriately, the court may make an order removing that director from office[FN22] and may fill that vacancy with a new director.[FN23]

The rationale for the proposed section **11.5** of the *CCAA* is explained in Industry Canada's clause by clause analysis of *Statute c. 47*.[FN24] Industry Canada said that directors of a corporation under *CCAA* protection are in a strong position to positively or negatively impact the restructuring process. In contrast to a bankruptcy, directors retain the ability to manage the debtor's business and control the development of the proposal to creditors. Given that directors could abuse their position of power, section **11.5** is "intended to provide shareholders, creditors and other stakeholders with the opportunity to quickly address problematic situations."[FN25]

At present, new section **11.5** is dormant. *Statute c. 47* has been subject to delayed proclamation since it received Royal Assent on November 25, 2005.[FN26] In its November 24, 2005 review of *Statute c. 47*, the Senate Committee identified corporate "governance" as an area in need of further study.[FN27] However, the 2007 amendments to Statute c.47 did not alter the wording of section **11.5** of the *CCAA*.[FN28]

4. — The United Kingdom Director Disqualification Regime

The UK director disqualification regime provides a point of comparison for the Canadian *Statute c. 47* reform. English courts have had the statutory power to disqualify directors involved in the management of insolvent companies since the enactment of the *Insolvency Act 1976*.[FN29] The law, as amended, is now contained in the *Company Directors Disqualification Act 1986* (the "*CDDA*").[FN30] The purpose of the law is to protect the public interest from unfit conduct by directors.[FN31]

Section 6(1) of the *CDDA* gives the court authority to disqualify any person who is or has been a director of an insolvent company, or a company that subsequently became insolvent, where the court decides his conduct as a director of that company, either taken alone or together with his conduct as a director of any other company, makes him unfit to be involved with the management of a company.[FN32] A number of guidelines are provided in Part I and II of the Schedule of the *CDDA* to help the court determine if a director's conduct is unfit. Under section 9, the court should have particular regard to these guidelines, but may also ground a disqualification order on factors not specifically listed.[FN33]

The effect of a disqualification order is to prohibit the disqualified person, without leave of the court, from acting as a director of any company or engaging in the promotion, formation or management of any company for a period of time decided by the court.[FN34] Contravention of a disqualification order is a criminal offence with a maximum penalty of two years imprisonment and a fine[FN35] and can also result in personal liability for company debts.[FN36]

5. — Problems with Chapter 47's Director Removal Regime

As currently drafted, there are a number of problems in *Statute c. 47*'s director removal scheme. Four major criticisms of the proposed *CCAA*, section **11.5** are discussed below.[FN37] Recommendations for improvement are also discussed.

(a) — Interference in Debtor's Business Judgment

The court's power to remove and replace a director interferes with Canada's system of corporate governance. The *CBCA* and its provincial equivalents currently govern the election, appointment and removal of directors. Shareholders are given the specific power to elect and remove directors.[FN38] Existing directors may fill vacancies that occur on the board of directors pending the next general shareholder meeting.[FN39]

The Court of Appeal in *Stelco* held that the appointment of the new directors was a corporate governance decision that was "no more within the purview of the court's knowledge and expertise than other business decisions, and [it] deserve[d] the same deferential approach."[FN40] Although the Court acknowledged that where there has been "more than some risk of anticipated misconduct," the oppression remedy provisions of the *CBCA* could be imported into the *CCAA* through section 20 of the *CCAA* to allow court removal of directors,[FN41] Justice Blair emphasized this is an exceptional remedy that is rarely used in corporate law.[FN42] He did not identify a single case where the remedy has been used to remove a director of a debtor corporation under *CCAA* protection.[FN43]

It is difficult to determine how the proposed section **11.5** of the *CCAA* will interfere with Canada's system of corporate governance. This is, in part, because the effects of a removal order are not explained in *Statute c. 47*. It is not clear if a removal order under new section **11.5** will have the effect of permanently removing a director from office or if a director will be able to apply for reappointment after *CCAA* proceedings come to an end. If a director is removed and subsequently replaced, is the replacement only for the duration of the restructuring process? Furthermore, will a court-appointed director incur the same obligations and liabilities as directors elected or appointed under the *CBCA* and its provincial equivalents?[FN44] It is also not clear if a director removed from office could be prohibited from acting as a director of other corporations beyond the debtor corporation.

The UK disqualification regime provides more explicit guidelines than *Statute c. 47*. Section 6(4) of the *CDDA* limits the disqualification period to a minimum of two years and maximum of fifteen years. Although a finding of unfitness results in a mandatory order of disqualification for at least two years, judges retain considerable discretion to determine unfitness in the first place. In addition, a disqualified director may apply to the court for leave to appeal the order[FN45] or modify its effect.[FN46]

(b) — Imperfect Predictions of Future Conduct

The proposed section **11.5** of the *CCAA* follows recommendation no. 35 in the 2003 Senate Standing Committee report, which proposed to give the court the authority under the *CCAA* to replace directors when the governance structure "is impairing" the restructuring process.[FN47] However, the proposed section **11.5** goes further in allowing the court to consider if the director is "likely to unreasonably impair" a viable restructuring or is "likely to act inappropriately."[FN48] If courts are vested with this discretion to make predictions about a director's future actions, the interpretation of the proposed section **11.5** could be driven by inconsistency. Courts would engage in a speculative and therefore imperfect forecast of the director's capacity to contribute to a viable reorganization. In addition, a removal order substantially interferes with the director's freedom to engage in meaningful employment and ability to earn a living. Infringing on individual liberty is a serious issue and such an infringement should not be based on speculative reasoning.

The Report on the Commercial Provisions of *Statute c. 47*, by the Legislative Review Task Force (the "LRTF") supported director removal to the extent that the director had "unreasonably impaired" the restructuring process.[FN49] The LRTF recommended that removal orders based on anticipated future misconduct should be granted "cautiously" and "only in the clearest of cases." In addition, the LRTF questioned whether it is appropriate as a matter of public policy to give the court the responsibility and power to speculate about the future conduct of directors.[FN50]

Anticipated future misconduct is not relevant to a finding of unfitness under the UK director disqualification regime. There is no mention of future misconduct in section 6 or in Part I and II of the Schedule to the English *CDDA*. Section 6 of the *CDDA* specifically says a director will be disqualified where his "conduct" makes him unfit. Furthermore, in *Re Bath Glass Ltd.* Justice Gibson said that to determine unfitness:[FN51]

> [w]hat the court must have regard to is the director's conduct; that is a term of great generality and I do not doubt that it was deliberately so chosen. The court must be satisfied that the conduct in question is sufficiently serious to lead it to the conclusion that the director is unfit . . . .

(c) — Lack of Guidance

Unlike in Part I and II of the Schedule to the English *CDDA*, *Statute c. 47* does not provide additional guidance to assist the court in determining if a director should be removed from office. As a result, Canadian courts will be left to devise their own rules of interpretation. Although this will allow for a flexible test that is easily adapted to unique fact patterns, it will inevitably cause inconsistency in the degree of culpability required before removal is ordered.[FN52] Directors will also be left unclear about their statutory obligations under the proposed section **11.5** and the means necessary to avoid removal. This uncertainty may have the effect of encouraging competent directors to resign from boards of insolvent corporations either before or during reorganization proceedings.

The Insolvency Institute of Canada's ("IIC") report on *Statute c. 47* recognized that the test articulated in the proposed section **11.5** could be interpreted as a "bad apple" test, where courts look to the bad conduct or anticipated bad conduct of an individual director.[FN53] The IIC suggested an amendment to the proposed section **11.5**, which required the court to focus instead on the overall governance of the debtor corporation. The IIC explained that when the majority of insolvent corporations enter protection under the *CCAA*, a controlling shareholder or shareholder group is present. Accordingly, a successful restructuring may require the controlling shareholder to surrender its control to an independent party early in the process.[FN54]

The IIC's approach to the proposed section **11.5** interpretation is similar to the determination of unfitness under the UK disqualification regime. English courts have held that evidence of general mis-behaviour should not be considered in a finding of unfitness. Only conduct in respect of company mismanagement is relevant to the analysis under section 6 of the *CDDA*.[FN55]

In addition to statutory guidelines, a detailed policy rationale explaining the primary objectives of removing a director from office would assist the court and directors in determining the standards of conduct required. English case law has repeatedly asserted the primary rationale for disqualifying a director is to protect the public interest, not to punish the director.[FN56] Given this purpose, in the English case *Re Grayan Building Services Ltd.*, Henry LJ explained, "the court's focus should be on [director's] conduct — on the offence rather than the offender."[FN57] A more detailed rationale for the proposed section **11.5** of the *CCAA* would give the court a basis from which to assess the director's capacity to contribute to a viable restructuring.

(d) — Long and Expensive Proceedings

According to Industry Canada's clause by clause analysis of *Statute c. 47*, the purpose of the proposed section **11.5** is to provide a remedy that efficiently protects the interests of corporate stakeholders in *CCAA* proceedings.[FN58] Industry Canada referred to *Stelco* as an example of where the *CCAA* is "neither efficient nor flexible enough" to resolve disputes "in a timely manner."[FN59]

Although it is difficult to gauge if the proposed section **11.5** of the *CCAA* will be an efficient remedy for corporate stakeholders, the UK experience under section 6 of the *CDDA* suggests the remedy could be procedurally inefficient. Since the enactment of section 6 of the *CDDA* in 1986, English judges have expressed concern about the amount of time it takes to enforce remedies under section 6.[FN60] In *Re Westmid Packing Services Ltd.*, Lord Woolf M.R., for the English Court of Appeal, acknowledged "there is often a considerable time lag between the conduct complained of, its discovery and the disqualification proceedings actually coming to court."[FN61] Lord Woolf M.R. attributed this delay to "over-elaboration in the preparation and hearing of these cases and a technical approach as to what evidence is and is not admissible."[FN62]

The enactment of section 6 of the *CDDA* also caused "an explosion of litigation" in the UK, which further delayed proceedings[FN63] and increased costs.[FN64] Removal applications under section **11.5** of the *CCAA* could be subject to similar expensive delays, depending on the magnitude of applications received.

Rather than committing time and money to enforce remedies under section **11.5** of the *CCAA*, a more efficient solution may be to authorize the court to appoint an interim "manager" to run the restructuring proceedings while existing management remains in place. This alternative has received support from both the LRTF[FN65] and the IIC.[FN66] In addition, some English judges have sought to reduce rising costs and mounting delays by allowing summary procedures[FN67] or legally binding undertakings.[FN68] Allowing similar procedures in Canada would help section 11.5's efficiency objectives. Also, if the procedure for removing a director under section **11.5** of the *CCAA* is by way of application rather than action, the remedy could be faster and less expensive to obtain.

6. — Should Section 11.5 be Proclaimed into Canadian Insolvency Law?

A number of recommendations to reduce the detrimental effects of the proposed section **11.5** of the *CCAA* were provided in Part 4 of this article. One option would be to adopt the proposed section **11.5** with amendments similar to those stated above. Many of these changes would bring section **11.5** more closely in line with the UK director disqualification regime. Industry Canada, in the 2001 report "Efficiency and Fairness in Business Insolvencies", endorsed the UK disqualification regime as an efficient and effective means of deterring director misconduct. Industry Canada stated:[FN69]

> The disqualification provisions — n important feature distinguishing the UK regime from its Canadian and U.S. counterparts — weed out incompetent directors to some extent and help to curb abuse and reinforce confidence in the integrity of the corporate and insolvency systems.

Thus, an amended section **11.5** could better protect stakeholder interests without dissuading competent individuals from acting as directors during *CCAA* proceedings.

The better argument, however, is that the proclamation of the proposed section **11.5** is not necessary, since the objectives of the proposed section **11.5** are sufficiently met within the existing *CCAA* framework. This is for the following three reasons. First, while directors retain control of the debtor corporation at the commencement of *CCAA* proceedings, independent court-appointed officers work on behalf of all stakeholders to prevent conflicts of interest and encourage good governance. In all cases, a monitor must be appointed as part of the initial stay order to supervise the business and affairs of the debtor and make sure that management does not prejudice the interests of any stakeholder.[FN70] Where stakeholders have lost confidence in management's ability to reorganize, the monitor may help negotiate a viable plan or arrangement between the debtor and its creditors.[FN71] As well, creditors may apply to have an interim receiver[FN72] or chief restructuring officer[FN73] appointed to replace existing management and assume control of the corporation. Alternatively, rather than waiting for a court-order, creditors and stakeholders may use their bargaining power to enforce the removal of one or more directors as a condition in a proposed reorganization plan.[FN74]

Creditors have sometimes expressed concerns that monitors selected by the debtor corporation might advance the interests of the debtor rather than the interests of the stakeholders.[FN75] In response, Canadian courts have consistently confirmed that monitors are independent officers of the court and have a duty to act independently to consider and balance the interests of all stakeholders in the *CCAA* proceeding.[FN76] If *Statute c. 47* is proclaimed into force, the new section 11.7 of the *CCAA* will place additional restrictions on who can become a monitor and will provide increased protection to stakeholder interests.[FN77]

Second, although the Ontario Court of Appeal in *Stelco* held that section 11 of the *CCAA* does not currently give the court the authority to remove directors of a debtor corporation, the Court recognized that the oppression remedy provisions of the *CBCA* and its provincial equivalents may be imported into section 11 discretion through section 20 of the *CCAA* to allow the court to remove directors in certain situations. The Court emphasized that at least "more than some risk of anticipated misconduct" would be necessary for director removal under the oppression remedy.[FN78] While this test represents a higher degree of director culpability than is required under proposed section **11.5** of the *CCAA*, the oppression remedy is but one of the options available to protect stakeholders and encourage good governance in *CCAA* proceedings.

When considering the application of the oppression remedy, the Court in *Stelco* endorsed the proposition that "altering a board of directors should be *a measure of last resort*."[FN79] The higher threshold under the oppression remedy is a less intrusive means of interfering with Canada's system of corporate governance and better promotes certainty and fairness in *CCAA* proceedings, since more than a prediction of future misconduct is required before removal can be ordered.

Finally, in addition to the obligations on directors under the oppression remedy, directors owe a fiduciary duty under section 122(1)(a) of the *CBCA* to act honestly and in good faith with a view to the best interests of the corporation and a duty of care under section 122(1)(b) of the *CBCA* to exercise care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. In *Peoples*, the Supreme Court of Canada recognized that the beneficiary of the duty of care under section 122(1)(b) of the *CBCA* is open-ended and must include creditors.[FN80] In addition, although the Supreme Court held that directors of financially distressed corporation owe their fiduciary duty to the corporation alone, in determining the best interests of the corporation under section 122(1)(a), directors may consider the interests of "shareholders, employees, suppliers, creditors, consumers, governments and the environment."[FN81] The Supreme Court continued that where a corporation is financially troubled, directors must "be careful ... not to favour the interests of any one group of stakeholders."[FN82] Thus, stakeholders of insolvent corporations may have this additional means to hold directors accountable for their conduct during restructuring proceedings.[FN83]

7. — Conclusion

There are serious flaws in *Statute c. 47*'s proposed director removal scheme. The proposed section **11.5** of the *CCAA* would interfere with the business judgment of corporations and uses an unreasonably low standard that could lead to director removals based on speculation. In addition, the lack of guidance as to when a director should be removed would likely lead to inconsistent decisions and uncertainty among current directors. Finally, based on the UK experience, the proposed remedy could be procedurally inefficient and expensive.

While certain amendments could be made to the proposed provision, the better approach is to shelve *Statute c. 47*'s director removal scheme. The objectives of the proposed *CCAA*, section **11.5** are better served by the existing Canadian statutory framework.

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FN2. R.S.C. 1985, c. C-36, amended S.C. 1997 [*CCAA*].

FN3. *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, S.C. 2005, c. 47 (not yet in force) [*Statute c. 47*]. *Statute c. 47* was derived from Bill C-55, which received royal assent on Friday November 25, 2005, but was not proclaimed into law. In 2007, Bill C-62 and Bill C-12 proposed several technical and substantive amendments to *Statute c. 47*. With no further amendments by the Senate, on December 14, 2007, Bill C-12 became *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 (not yet in force) [*Statute c. 36*].

FN4. *CCAA*, *supra*, n. 1, s. **11.5** (not yet in force). Section **11.5** was not among the *CCAA* provisions amended in 2007 by *Statute c. 36* and remains as stated in *Statute c. 47*. *Statute c. 47* also gives the court the authority to remove directors under new s. 64 (not yet in force) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, amended S.C. 1997, c. 12. However, this article will focus in particular on the removal of directors under the *CCAA*, since the largest and most complex restructurings in Canada occur in *CCAA* proceedings. Janis P. Sarra stated in *Rescue! The Companies' Creditors Arrangement Act* (Toronto: Carswell, 2007) at 1, that the *CCAA* "has been the statute of choice for debtor corporations in every major restructuring in the past quarter century, including national airlines, major steel and forestry companies, telecommunications companies and the national blood delivery system."

FN5. *Stelco Inc., Re* (2005), [2005] O.J. No. 1171, 2005 CarswellOnt 1188, 75 O.R. (3d) 5, 2 B.L.R. (4th) 238, 9 C.B.R. (5th) 135, 196 O.A.C. 142, 253 D.L.R. (4th) 109 at para. 32 (Ont. C.A.) [*Stelco*]. See also *Babcock & Wilcox Canada Ltd., Re* (2000), [2000] O.J. No. 786, 2000 CarswellOnt 704, 5 B.L.R. (3d) 75, 18 C.B.R. (4th) 157 at para. 11 (Ont. S.C.J. [Commercial List]); *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 1990 CarswellBC 394, [1990] B.C.J. No. 2384, 51 B.C.L.R. (2d) 84, 4 C.B.R. (3d) 311 at 320, [1991] 2 W.W.R. 136 (B.C. C.A.); *Lehndorff General Partner Ltd., Re* (1993), 1993 CarswellOnt 183, [1993] O.J. No. 14, 17 C.B.R. (3d) 24, 9 B.L.R. (2d) 275 (Ont. Gen. Div. [Commercial List]).

FN6. *Stelco*, *ibid.*, at para. 32. See also *Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106, 1995 CarswellOnt 54, [1995] O.J. No. 595 (Ont. Gen. Div. [Commercial List]); *Royal Oak Mines Inc., Re* (1999), 1999 CarswellOnt 792, [1999] O.J. No. 864, 7 C.B.R. (4th) 293 (Ont. Gen. Div. [Commercial List]); *Westar Mining Ltd., Re*, 1992 CarswellBC 508, 70 B.C.L.R. (2d) 6, 14 C.B.R. (3d) 88, [1992] 6 W.W.R. 331 (B.C. S.C.).

FN7. *Stelco*, *supra*, n. 4 at para. 86. See also *Skeena Cellulose Inc., Re*, 2003 CarswellBC 1399, [2003] B.C.J. No. 1335, 2003 BCCA 344, 184 B.C.A.C. 54, 302 W.A.C. 54, 43 C.B.R. (4th) 187, 13 B.C.L.R. (4th) 236 (B.C. C.A.); *Sammi Atlas Inc., Re* (1998), 3 C.B.R. (4th) 171, 1998 CarswellOnt 1145, [1998] O.J. No. 1089 (Ont. Gen. Div. [Commercial List]); *Olympia & York Developments Ltd. v. Royal Trust Co.* (1993), 1993 CarswellOnt 182, [1993] O.J. No. 545, 17 C.B.R. (3d) 1, 12 O.R. (3d) 500 (Ont. Gen. Div.); *Alberta-Pacific Terminals Ltd., Re* (1991), 8 C.B.R. (3d) 99, 1991 CarswellBC 494, [1991] B.C.J. No. 1065 (B.C. S.C.).

FN8. 2004 CarswellQue 2862, 2004 CarswellQue 2863, [2004] S.C.J. No. 64, REJB 2004-72160, 326 N.R. 267 (Eng.), 326 N.R. 267 (Fr.), 4 C.B.R. (5th) 215, [2004] 3 S.C.R. 461, 2004 SCC 68, 244 D.L.R. (4th) 564, 49 B.L.R. (3d) 165 (S.C.C.) at para. 67 [*Peoples*].

FN9. (1991), [1991] O.J. No. 683, 1991 CarswellOnt 133, 1 B.L.R. (2d) 225, 3 O.R. (3d) 289, 45 O.A.C. 320, 80 D.L.R. (4th) 161 (Ont. C.A.) at para. 74.

FN10. Stelco entered protection under the *CCAA* on January 29, 2004. *Stelco*, *supra*, n. 4 at para. 1.

FN11. The new directors had been validly appointed the week before, in accordance with s. 111 of the *CBCA*, to replace vacancies on the Board.

FN12. See L.W. Houlden, G.B. Morawetz & Janis Sarra, *Bankruptcy and Insolvency Law of Canada*, 3rd ed. (Toronto: Carswell, 2005) rev. vol. 4 at 10A-36.6.

FN13. *Stelco Inc., Re* (2005), [2005] O.J. No. 730, 2005 CarswellOnt 743, 7 C.B.R. (5th) 310 (Ont. S.C.J. [Commercial List]); reversed (2005), [2005] O.J. No. 1171, 2005 CarswellOnt 1188, 253 D.L.R. (4th) 109, 75 O.R. (3d) 5, 2 B.L.R. (4th) 238, 9 C.B.R. (5th) 135, 196 O.A.C. 142 (Ont. C.A.).

FN14. R.S.C. 1985, c. C-44 [*CBCA*].

FN15. *Stelco*, *supra*, n. 4 at para. 70.

FN16. *Ibid.*, at para. 61.

FN17. Industry Canada, "Bill C-55: clause by clause analysis, Bill Clause No. 128 Section No. **11.5**. Topic: Removal of Directors," online: <http://strategis.ic.gc.ca/epic/site/cilppdci. nsf/en/h cl00790e.html>.

FN18. For additional comments on *Stelco* see: John D. Honsberger & Vern DaRe, *Debt Restructuring Principles and Practice* (Aurora: Canada Law Book, 1990) vol. 1 at 9-58; L.W. Houlden, G.B. Morawetz & Janis Sarra, *Bankruptcy and Insolvency Law of Canada*, 3rd ed. (Toronto: Carswell, 2005) rev. vol. 4 at 10A-36.6; Richard H. McLaren, *Canadian Commercial Reorganization Preventing Bankruptcy*, (Aurora: Canada Law Book, 1994) vol. 1 at 2-30.11.

FN19. See also *Skeena Cellulose Inc., Re*, 2003 CarswellBC 1399, [2003] B.C.J. No. 1335, 2003 BCCA 344, 184 B.C.A.C. 54, 302 W.A.C. 54, 43 C.B.R. (4th) 187, 13 B.C.L.R. (4th) 236 (B.C. C.A.) at para 46; *GMAC Commercial Credit Corp. — Canada v. TCT Logistics Inc.*, 2006 CarswellOnt 4621, 2006 CarswellOnt 4622, [2006] S.C.J. No. 36, 51 C.C.E.L. (3d) 1, 22 C.B.R. (5th) 163, 53 C.C.P.B. 167, [2006] 2 S.C.R. 123, 215 O.A.C. 313, 2006 SCC 35, 351 N.R. 326, 2006 C.L.L.C. 220-045, 271 D.L.R. (4th) 193 (S.C.C.); Michael J. MacNaughton & Magnus C. Verbrugge, "Jurisdiction, Discretion, and the Road Followed: The Supreme Court of Canada's Decision in *TCT Logistics*" (2006) Ann. Rev. Insol. L. 235 at 275; Ronald B. Davis, "The Way Forward: Policy Implications of the Supreme Court Decision in TCT Logistics" (2007) 44 C.B.L.J. 357.

FN20. This position was acknowledged in *Pacific Coastal Airlines Ltd. v. Air Canada*, 2001 CarswellBC 2943, [2001] B.C.J. No. 2580, 2001 BCSC 1721, 19 B.L.R. (3d) 286 (B.C. S.C.) at para. 24 [*Pacific*]; and was further accepted in *Stelco Inc., Re* (2005), 2005 CarswellOnt 6818, [2005] O.J. No. 4883, 204 O.A.C. 205, 78 O.R. (3d) 241, 261 D.L.R. (4th) 368, 11 B.L.R. (4th) 185, 15 C.B.R. (5th) 307 (Ont. C.A.); additional reasons at (2006), 2006 CarswellOnt 5194 (Ont. C.A.).

FN21. See E. Patrick Shea, *Bankruptcy & Insolvency Act, Companies' Creditors Arrangement Act, Bill C-55 & Commentary* (Markham: LexisNexis Butterworths, 2006). Bill C-55 is not the first proposal to deal with sanctions for director misconduct in insolvency situations. See *Report of the Study Committee on Bankruptcy and Insolvency Legislation* (Canada: 1970) at 3.2.027; *Proposed Bankruptcy Act Amendments Report of the Advisory Committee on Bankruptcy and Insolvency*, (Ottawa: Minister of Supply and Services Canada, 1986) at 113 to 115.

FN22. *CCAA*, s. **11.5**(1) (not yet in force).

FN23. *CCAA*, s. **11.5**(2) (not yet in force).

FN24. *Supra*, n. 16.

FN25. *Ibid.*

FN26. Bill C-55 was pushed through the House of Commons and Senate with little review to ensure its passing before the January 23, 2006 federal election. As a result, the Senate Committee obtained an assurance from the federal government that *Statute c. 47* would not be proclaimed into force before June 30, 2006, at the earliest, to allow time for a detailed and thorough review. Standing Committee on Banking Trade and Commerce, *Seventeenth Report* (on Bill C-55, 2005), 24 November 2005 [Standing Committee]. See Jacob S. Ziegel, "The Travails of Bill C-55" (2005) 42 C.B.L.J. 440.

FN27. Standing Committee, *ibid.*

FN28. See Bill C-62, which was passed by the House of Commons on June 14, 2007 and Bill C- 12, which was passed by the House of Commons on October 29, 2007 and is now *Statute c. 36*, *supra*, n. 2. For information on the origins of Canadian statute-based sanctions for director misconduct that is harmful to stakeholders during insolvency situations see Industry Canada, *Efficiency and Fairness in Business Insolvencies* (Corporate Law Policy Development, 2001) at 12-18.

FN29. (U.K), 1976, c. 60, s. 9.

FN30. (U.K.), 1986, c. 46, s. 6 [*CDDA*].

FN31. *CDDA*, *ibid.*, s. 7(1). In *Re Sevenoaks Stationers (Retail) Ltd.*, [1990] B.C.C. 765, [1991] Ch. 164 at 176 Dillon LJ said that s. 6 of the *CDDA* is designed to protect "in particular potential creditors ... from losing money through companies becoming insolvent when the directors of those companies are people unfit to be concerned with the management of a company." This purpose aligns with the recognition in English insolvency law that as a company approaches insolvency, the interests of creditors will supersede the interests of shareholders. See *Re Horsley Weight Ltd.*, [1982] Ch. 442, 3 All E.R. 1045; *Brady v. Brady*, [1989] A.C. 755, 2 All E.R. 617.

FN32. Section 6(2) of the *CDDA* defines an "insolvent" company in broad terms to include not only a company that is in liquidation, but also a situation where an administrative receiver of the company has been appointed or where an administration order has been made in relation to the company.

FN33. *Re Bath Glass Ltd.*, (1988) 4 B.C.C. 130, [1988] B.C.L.C. 329; *Re Churchill Hotel (Plymouth) Ltd.*, 1988 P.C.C. 220, [1988] B.C.L.C. 341.

FN34. *CDDA*, *supra*, n. 29 s. 1(1). Under this section, a disqualified director shall also not act as an administrator, liquidator or receiver of any company.

FN35. *Ibid.*, s. 13.

FN36. *Ibid.*, s. 15.

FN37. See also the 2008 submission by insolvency law academics, entitled "Submissions on Statute c.47 and Statute c.12: *The Wage Earner Protection Program Act*, and *Amendments to the Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act*, presented to the Standing Senate Committee on Banking, Trade and Commerce," which identified significant problems with the proposed s. 11.5 of the *CCAA* and objected to its enactment, at 38-40.

FN38. *CBCA*, *supra*, n. 13, ss. 106(3) and 109(1).

FN39. *Ibid.*, s. 111.

FN40. *Stelco*, *supra*, n. 4 at para. 70. In reaching this conclusion, the Court of Appeal, at paragraph 65, relied on the Supreme Court of Canada's acknowledgment in *People's Department Stores v. Wise* that courts should be very hesitant to interfere in corporate governance decisions made by directors and management.

FN41. *Ibid.*, at para. 53.

FN42. *Ibid.*, at para. 51.

FN43. For further information regarding the judiciary's general reluctance to interfere with business judgment, see Janis Sarra, "Canada's Supreme Court rules no fiduciary obligation towards creditors on insolvency — Peoples Department Stores v. Wise" (2006) 15 INSOL Int'l. Insol. Rev. 1; Stephanie Ben-Ishai, "A Team Production Theory of Canadian Corporate Law" (2006) 44 Alta. Law Rev. 2.

FN44. This question was raised in Brian M. Hunt & Rish Handa, "A Critical Comparison Between Australian and Canadian Creditor Protection Regimes: Voluntary Administration and the CCAA" (2006) Ann. R. Ins. L. 895 at 924.

FN45. *CDDA*, *supra*, n. 29, s. 17.

FN46. See *Secretary of State v. Worth*, [1994] B.C.C. 371, [1994] 2 B.C.L.C. 113; David Milman & Chris Durrant, *Corporate Insolvency: Law and Practice*, 3rd ed. (London: Sweet & Maxwell, 1999) at 253 [Milman].

FN47. *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act*, Report of the Standing Senate Committee on Banking, Trade and Commerce, November 2003 at 149-150.

FN48. See Legislative Review Task Force (Commercial) of the Insolvency Institute of Canada and the Canadian Association of Insolvency and Restructuring Professionals, *Report on the Commercial Provisions of Bill C-55* at 51.

FN49. *Ibid.*, at 11.

FN50. *Ibid.*, at 52.

FN51. *Supra*, n. 32 at para. 12.

FN52. Although the UK director disqualification regime contains specific statutory guidelines, case law under *CDDA*, s. 6 has been characterized as "a wilderness of single instances". Francis Fitzpatrick, "Disqualification of a Director on grounds of Unfitness" (1992) 142 New L.J. 596. In addition, it has been recognized that the criteria for determining unfitness under CDDA s. 6 vary between the reported decisions. See Andrew McGee & Christina Williams, *The Business of Company Law*, (Oxford: University Press, 1995) at 303; Milman, supra, n. 45 at 244.

FN53. *Position Paper Bill C-55* (Insolvency Institute of Canada, 2005) at 3-4.

FN54. *Ibid.*, at 4.

FN55. *Re Dawes and Henderson Agency*, [1997] 1 B.C.L.C. 329, 1996 WL 1093403 (Ch. Div.); *Re Westmid Packing Services Ltd. (Secretary of State v. Griffiths)*, [1998] 2 B.C.L.C. 646, 2 All E.R. 124; Milman, *supra*, n. 45 at 245.

FN56. *Re Rolus Properties Ltd.*, (1988) 4 B.C.C. 446, 1986 WL 1165464 (Ch. Div. (Companies Ct)); Milman, *supra*, n. 45 at 244.

FN57. 1 B.C.L.C. 276, [1995] B.C.C. 554 at 577.

FN58. *Supra*, n. 16.

FN59. *Ibid.*

FN60. Milman, *supra*, n. 45 at 252.

FN61. [1998] 2. B.C.L.C. 646, 2 All E.R. 124 at para 3.

FN62. *Ibid.*, at para. 9.

FN63. Milman, *supra*, n. 45 at 244; The UK Department of Trade and Industry 1996 year-end statistics (published on 7 February 1997) show that the total number of disqualification orders against unfit directors in the UK was 633 in 1995 and increased by over 49% to 946 in 1996, cited in Stephen Griffin, *Personal Liability and Disqualification of Company Directors* (Oxford and Portland, Oregon: Hart Publishing, 1999) at 149.

FN64. The annual cost of resources invested in the UK director disqualification regime for the year 1997-1998 was estimated at £22 million. National Audit Office Follow-up Report (HC 1998-99, No. 424), cited in Milman, *supra*, n. 45 at 256. While the UK director disqualification regime is more developed than the Bill C-55 scheme, this figure provides an example of possible public expenditure implications.

FN65. *Supra*, n. 47 at 52.

FN66. *Supra*, n. 52 at 4.

FN67. This procedure was first allowed by Ferris J. in *Re Carecraft Construction Co Ltd.*, [1993] B.C.C. 336, [1994] 1 W.L.R. 172.

FN68. See *Re Homes Assured Corporation plc.*, [1996] B.C.C. 297, 1996 WL 1093335 (Ch. Div.); *Secretary of State v. Cleland*, [1997] B.C.C. 473, 1 B.C.L.C. 437.

FN69. *Supra*, n. 27 at 16.

FN70. *CCAA*, *supra*, n. 1, ss. **11.5** and 11.7. The functions of a monitor are set out in s. 11.7(3) of the *CCAA*. See Sarra, *supra*, n. 3 at 260. *Statute c. 47* proposes to place new restrictions on who can become a monitor (new *CCAA*, s. 11.7, not yet in force) and clarify the role of monitors in *CCAA* proceedings (new *CCAA*, s. 23(1), not yet in force).

FN71. *CCAA*, *supra*, n. 1, s. 11.7(3); and see Sarra, *ibid.*, at 268.

FN72. See *General Electric Capital Canada Inc. v. Euro United Corp.* (1999), 1999 CarswellOnt 4908, 25 C.B.R. (4th) 250 (Ont. S.C.J. [Commercial List]). In some situations, the monitor may also be appointed as an interim receiver to replace management and assume control of the restructuring process. See *Royal Oak Mines Inc., Re*, (1999), [1999] O.J. No. 1369, 11 C.B.R. (4th) 122, 1999 CarswellOnt 1068 (Ont. Gen. Div. [Commercial List]).

FN73. See *Ivaco Inc., Re* (2004), 3 C.B.R. (5th) 33, 2004 CarswellOnt 2397 (Ont. S.C.J. [Commercial List]); *Consumers Packaging Inc., Re* (2001), 2001 CarswellOnt 3331, [2001] O.J. No. 3736, 27 C.B.R. (4th) 194 (Ont. S.C.J. [Commercial List]); leave to appeal refused (2001), 2001 CarswellOnt 3482, [2001] O.J. No. 3908, 150 O.A.C. 384, 27 C.B.R. (4th) 197, 12 C.P.C. (5th) 208 (Ont. C.A.).

FN74. See Sarra, *supra*, n. 3 at 128.

FN75. *Ibid.*, at 261.

FN76. *Hickman Equipment (1985) Ltd., Re* (2002), 642 A.P.R. 126, 214 Nfld. & P.E.I.R. 126, 34 C.B.R. (4th) 203, 2002 CarswellNfld 154 (Nfld. T.D.); *Siscoe & Savoie v. Royal Bank* (1994), 404 A.P.R. 42, 157 N.B.R. (2d) 42, 1994 CarswellNB 14, 29 C.B.R. (3d) 1 at para. 28 (N.B. C.A.); leave to appeal to S.C.C. refused (1995), 32 C.B.R. (3d) 179n (S.C.C.); *Re Royal Oak Mines Inc.* (1999), *supra*, n. 71.

FN77. *CCAA*, *supra*, n. 1, s. 11.7 (not yet in force). Also, *Statute c. 47* proposes new *CCAA*, s. 23(1) (not yet in force), which clarifies the duties of monitors and reduces changes of conflicts.

FN78. *Stelco*, *supra*, n. 4 at para. 61.

FN79. *Ibid.*, at para. 55.

FN80. *Supra*, n. 7 at para. 57.

FN81. *Ibid.*, at para. 42.

FN82. *Ibid.*, at para. 47.

FN83. See Sarra, *supra*, n. 3 at 132.

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