REGIONAL DEVELOPMENTS

Canada*

In 1992, significant developments occurred in Canada in the bankruptcy and insolvency field and, of note to commercial lawyers, the United Nations Convention for International Sale of Goods Contracts came into force.

I. The New Bankruptcy and Insolvency Act

At the end of June, the Canadian legislature enacted a new federal Bankruptcy and Insolvency Act that will come into force upon proclamation by the Governor in Council, expected in December.

The presently existing, and soon to be replaced, Bankruptcy Act contains a major defect in that it is not binding upon secured creditors. Accordingly, a debtor company has been required to take advantage of the Companies' Creditors Arrangement Act (CCAA), which is somewhat like chapter 11 of the U.S. Bankruptcy Code. But, the CCAA is a very short piece of legislation that gives courts great discretion in dealing with the debtor company and the various classes of secured and unsecured creditors. As a result, a large field of inconsistent and uncertain jurisprudence has developed.

The new Bankruptcy and Insolvency Act provides a legislative framework somewhat similar to chapter 11 of the U.S. Bankruptcy Code. The new law permits the debtor company to present a reorganization plan to its debtors under court supervision and subject to ultimate creditor and court approval. Under the new legislation, a debtor can initiate the reorganization process either by filing a notice of intention to make a proposal or by filing the actual proposal it wishes to make to its creditors.

If the debtor files a notice of intention, it has thirty days to file the proposal.

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The time period may be extended for additional periods of up to forty-five days, but the total of all extended time periods may not exceed five months. A creditor may oppose an extension on various grounds, including that the creditors' agreement to a proposal will not happen within the time limits, or at all.

Within ten days after filing a notice of intention to make a proposal, the debtor must file a projected cash flow with its own report and a report from the trustee on the reasonableness of the projected cash flow. These reports will assist creditors and the court in assessing the viability of the proposed reorganization.

During the proposal process, the new Act will grant the debtor a broad automatic stay of proceedings that is binding on all creditors of the debtor, including secured creditors. A creditor may apply to the court to have the stay lifted; however, the court must be satisfied that the creditor is likely to be materially prejudiced by the continued stay or that lifting the stay is otherwise fair.

The Act has other provisions that were developed to facilitate commercial reorganization. For example, simply because the debtor has filed a notice of intention or a proposal, does not allow any person to terminate or amend an agreement with the debtor, or to claim an accelerated payment. However, the Act does not prevent a supplier from requiring payments on a C.O.D. basis, nor does it require anyone to make any further advances of money or credit to the debtor after the filing.

Finally, the new legislation outlines the procedure to be followed by creditors in evaluating the proposal. When the proposal is made, a creditors' meeting is called. At the meeting, all unsecured creditors and affected classes of secured creditors are entitled to vote by class. Unless the proposal provides for more than one class of unsecured claims, all unsecured creditors constitute one class. Secured creditors may be in one or more classes. The new Act provides that secured claims may be included in the same class if the interests of those creditors are sufficiently similar to give them a "commonality of interest." In addition, application may be made to the court to determine the appropriate classes of secured creditors.

For the proposal to receive approval a majority in number and two-thirds in value of the members of each class voting at the meeting must accept it. A proposal is effective if it is approved by the unsecured creditors and subsequently approved by the court. Even so, secured creditors of a class or classes that did not accept the proposal may proceed to realize on their security.

Termination of the proposal procedure will occur in the following instances: the debtor does not file a proposal within the required period after filing a notice of intent; the creditors reject the debtor's proposal; or in the event that the creditors accept the proposal filed by the debtor, the proposal is not approved by the court. In any such instance, the debtor is automatically deemed bankrupt as of the date the proceedings commenced, and secured creditors are free to realize on their security.

The procedure under the new Bankruptcy and Insolvency Act is more efficient than that found in the CCAA, which is often expensive and, as mentioned, unpredictable. While the CCAA will remain in effect, it will likely be used only for large, complex reorganizations due to the greater flexibility that the CCAA permits.

II. United Nations Convention on International Sale of Goods

The United Nations Convention on Contracts for the International Sale of Goods, 1980 (Convention) came into force in Canada on May 1, 1992. As of June 30, 1992, thirty-five countries had ratified the Convention including the United States, Germany, Australia, and France. While at present the Canadian provinces of Quebec, Saskatchewan, and the Yukon Territories are not parties to the Convention, their inclusion is expected.

The Convention applies only to commercial contracts for the sale of goods between parties whose places of business are in different countries if both countries have ratified the Convention. The Convention also applies when the rules of private international law dictate that the laws of the country or province that has ratified the Convention govern the contract. Therefore, an examination of existing contracts between Canadian businesses and firms located in other countries that have ratified the Convention could indicate that the contracts are already governed by the Convention. An exception to this rule applies in the case of contracting parties based in British Columbia, where the provincial legislation adopting the Convention contains a reservation concerning its application. For companies based in British Columbia, the Convention will only apply where the other party to the contract is located in a state that is also a party to the Convention. British Columbia's legislation adopting the Convention is the only Canadian legislation that restricts its applicability.

The terms of the Convention permit contracting parties to expressly exclude its application. Minor discrepancies exist in the various versions of the legislation passed by the provinces, the territories, and the federal government regarding how such an exclusion may be made; but in any event, each version permits the contracting parties either to stipulate a particular law, or expressly to exclude the applicability of the Convention. The legislation adopted by the various governments in Canada contain no other material differences.

Canada's decision to join the Convention is significant to its relationship with other countries that have already ratified it. For example, when the United States ratified the Convention, it made a similar reservation to that adopted by British Columbia, stating that the Convention will apply only to contracts where both the buyer and the seller are based in countries that have adopted the Convention. Accordingly, as long as Canada had not ratified the Convention, a contract between a Canadian and a U.S. company was not subject to the Convention, even if the parties chose U.S. law to govern their relationship. Since Canada has