Distressed Debt Lenders and their Impact on Restructurings and Workouts in Canada

Introduction

Restructuring proceedings and workouts in Canada have been impacted by a number of market factors over the course of the past several years, including changes in lending strategies and risk management by Canadian banks and other traditional cash flow lenders, the expansion of asset-based lending changing investment strategies leading to the availability of alternative sources of capital and the development of a secondary market for distressed debt.

There is no doubt that many businesses have become more sophisticated in terms of their capital structures and business operations. The resulting complexities, coupled with the factors referenced above, have compounded the challenges presented in a restructuring and workout context. At the same time, one could argue that these factors have created greater opportunities for creativity and the use of innovative approaches to address the needs of a restructuring business, particularly in terms of the restructuring of its balance sheet.

These developments have also given rise to the introduction of a number of new players in the Canadian restructuring marketplace. In this article, I will offer some perspectives on the impact which some of these new players have had in the Canadian lending market as well as in restructuring and workout proceedings, including debtor in possession (DIP) financing and other forms of “distressed” lending.
The Purchase and Sale of Distressed Debt

Following the trend in the United States which began several years ago, an active secondary market for the purchase of distressed debt has been developing in Canada over the past several years. It seems that, as the market for distressed debt in the U.S. has matured and the number of players has increased, many of those players have been looking north of the border for new opportunities. In this section, I will consider the impact which this has had in Canada from the perspective of corporate borrowers, lenders and the purchasers of distressed debt.

A. Existing Lenders

Prior to the development of an active debt trading market, the options available to a lender were somewhat limited. Assuming that inaction was not an acceptable option, the lender could either enforce its rights to recover its debt and liquidate the borrower’s collateral or take a longer term view and attempt to restructure in the hopes that its patience would be rewarded through restoration of the borrower to financial health and increased recovery at a future date. The lender’s decision could often be complicated by other factors ranging from “relationship” issues to the lender’s desire to continue providing other fee based services and, at times, even the management of the lender’s own balance sheet and income statement.

For the lender looking to make a quick exit from a troubled loan, liquidation was often seen as the more attractive of the two alternatives. Among other things, an earlier liquidation would reduce the professional costs and management time which would otherwise have to be expended and could also have desirable effects in terms of its impact on the lender’s capital requirements. Many traditional lenders historically operated with a “first loss is your best
loss” mentality. The downside was, of course, that this approach may well have lead to the premature demise of businesses which otherwise could have had an opportunity to restructure and continue.

In contrast to this, there certainly have been cases where a traditional relationship banker has been motivated to stick with a borrower for too long a period of time, when more proactive management of the situation would have been indicated. In many cases, this may only serve to delay the inevitable and can actually be counterproductive to a successful restructuring. While it may seem counterintuitive from the perspective of other stakeholders, an enforcement of security or liquidation of collateral can often be regarded as a restructuring by other means since it allows a purchaser an opportunity for a fresh start, often preserving employment and supplier relationships notwithstanding the demise of the original borrower.

From a lender’s perspective, the presence of an active secondary trading market creates an alternative to the two options mentioned above. This third alternative can be very attractive in a number of situations. A sale of the lender’s debt and underlying security (usually at a discount to par value) provides an opportunity for a quick exit from a troubled situation, reduces costs and management time which would otherwise have to be devoted to restructuring or enforcement and reduces the lender’s capital requirements. The opportunity for a quick exit comes without the necessity of a liquidation, which can sometimes have business or even political implications which go beyond the effect on the lender’s balance sheet. This option is all the more attractive to those institutions which do not have the depth of resources and experience required to successfully restructure troubled businesses.
B. Borrowers

From the perspective of a borrower, any change or potential change in a lending relationship can be a source of concern, particularly when it occurs at a critical point in time. For the borrower who has relied on an existing working relationship with an institutional lender, the prospect of a change in that relationship and the introduction of a new party can be intimidating in these circumstances. Many borrowers clearly prefer “the devil you know”. However, with the move away from traditional lending relationships dominated by Canadian banks to a broader, arguably more competitive market, coupled with the introduction of asset-based lending, these dynamics have changed.

Some borrowers have discovered, to their chagrin, that their asset-based lender may not have the appetite or patience to work through a complicated restructuring scenario, relying instead on the hope that they have counted and valued the collateral correctly so as to preserve the possibility of a quick exit without an attendant loss. In this scenario, the presence of a secondary market and other financing alternatives can be of critical importance to the borrower. The introduction of a new player with an appetite for and experience in dealing with restructurings and workouts as well as the resources and commitment to work out a troubled loan can in fact enhance the borrower’s prospects of survival through a successful restructuring.

This is not to suggest, however, that the introduction of distressed debt purchasers has been universally regarded as being favourable from the perspective of borrowers and other stakeholders. There have undoubtedly been situations in which purchasers of distressed debt have been motivated by a singular desire to maximize the return on their investments. There is a perception that, in some cases, this profit motive may have been pursued without regard to the
fate of the borrower’s business and the “social” aspects of restructuring that a traditional
relationship lender might have considered to be one of the guiding principles in any restructuring
or workout scenario. The fact is that a purchaser of debt in the secondary market may not have
the same incentive to stick with a troubled borrower as compared to a more traditional
relationship type lender. However, it is fair to say that there is often uncertainty in dealing with
an existing lender as well since, from the existing lender’s perspective, the prospect of a loss and
the internal and external politics associated therewith can sometimes skew the lender’s behaviour
(either accelerating or delaying the impact of a restructuring, depending on the circumstances).

C. Purchasers of Distressed Debt

There is no doubt that the more sophisticated purchasers of distressed debt who
are now active in the Canadian marketplace have a different mindset as compared to more
traditional institutional lenders. It is not surprising that the majority of such players are based in
the United States, given the size and depth of the capital markets in that country. With a larger
capital base and significant amounts of funds available for investment, many U.S. based
purchasers of distressed debt have been able to capitalize on the fact that there is significant
capital available from investors or funds who are chasing higher returns and prepared to accept
the associated increase in credit risk.

Many purchasers of distressed debt have been criticized as having a short term
rather than a long term perspective. Those that have been successful in generating double digit
or greater returns in a relatively short time horizon have undoubtedly earned the admiration and
respect of their investors. In so doing, however, they may have occasionally trampled on the
hopes and expectations of their borrowers or investees and the creditors and other stakeholders in those companies.

The expectations of these players in terms of investment objectives and time horizon influence their approach to and behaviour in a restructuring context. For example, in certain cases, the distressed debt purchaser might favour liquidation as opposed to a restructuring on the basis that it will provide an immediate return sufficient to satisfy its investment objectives. It is, of course, a far different matter to contemplate liquidation of collateral expected to generate a fifty percent recovery on the original face amount of the loan when the loan was purchased at a fraction of the original amount outstanding. In those circumstances, the distressed debt purchaser may be looking at a handsome profit whereas the existing lender would have been incurring at a loss.

Moreover, the distressed debt lender, having entered the market on this basis, will be acutely aware of its ability to continue to trade or “flip” the debt which it has acquired. Accordingly, a successful result may be defined by a re-sale of the purchased debt at an attractive premium over the initial purchase price in contrast to a longer term restructuring requiring more patience in the hopes of generating a similar or better return. It is not uncommon to see debt traded two or three times in a relatively short time frame. In this context, the distressed debt lender may be motivated to act in a way which is intended to preserve the liquidity of its investment and this can also have a significant impact on the course of a restructuring or workout.
D. Summary

A chart comparing the various factors discussed above, first from the perspective of a lender and, secondly, from the perspective of a borrower is set out below:

**Lender’s Perspective**

<table>
<thead>
<tr>
<th>Existing Lender</th>
<th>Distressed Debt Purchaser</th>
</tr>
</thead>
<tbody>
<tr>
<td>• relationship factor, past history and politics can be a distraction</td>
<td>• no history/relationship – focus is on the future</td>
</tr>
<tr>
<td>• “emotional” attachment can be a hindrance</td>
<td>• new, objective perspective</td>
</tr>
<tr>
<td>• workout/restructuring skills necessary</td>
<td>• specialized focus and skill set</td>
</tr>
<tr>
<td>• usually proactively involved</td>
<td>• can have active or passive investment strategy</td>
</tr>
<tr>
<td>• longer term perspective usually prevalent unless investment parameters change</td>
<td>• perspective may be short term (e.g. “flip” scenario) or longer term (restructure, “buy and hold”)</td>
</tr>
</tbody>
</table>

**Borrower’s Perspective**

<table>
<thead>
<tr>
<th>Existing Lender</th>
<th>Distressed Debt Purchaser</th>
</tr>
</thead>
<tbody>
<tr>
<td>• relationship factor can be a benefit or an obstacle</td>
<td>• perception that relationship is irrelevant in most cases</td>
</tr>
<tr>
<td>• “the devil you know” - or -</td>
<td>• uncertainty, lack of familiarity with institutional objectives and values - or - opportunity for a fresh start?</td>
</tr>
<tr>
<td>“the sum of all fears”?</td>
<td></td>
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</tbody>
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As can be seen from this comparison and the preceding discussion, there is no “one size fits all” answer. By their nature, insolvency and restructuring proceedings are dynamic and are influenced by a number of different variables which can have a profound impact on the course of the proceedings and resultant outcome.
Debtor in Possession Financing

Debtor in possession or DIP financing has, for many years, been a prominent and important feature in proceedings under chapter 11 of the United States Bankruptcy Code. The U.S. Bankruptcy Code includes detailed provisions with respect to DIP financing\(^1\) and an active and rather lucrative market for DIP lenders has developed as a result. In Canada, the absence of specific provisions in the *Companies’ Creditor Arrangement Act*\(^2\) (“CCAA”) and *Bankruptcy and Insolvency Act*\(^3\) (“BIA”) dealing with financing for the restructuring debtor has inhibited the development of an active market in this area. However, with the advent of increased restructurings under the CCAA over the past ten to fifteen years, a limited market has developed nonetheless. As was the case in other areas, such as asset-based lending and the development of a market for the purchase and sale of distressed debt, the development of DIP lending in Canada has been influenced by major financial institutions and other players who have long been active in the U.S. market and have now entered the Canadian market as well.

The smaller market in Canada provides significantly fewer opportunities for DIP financing. This, coupled with the lack of a statutory framework and codification of rules, including rules for the protection of both existing creditors and DIP lenders, has also served to limit the appetite of many players to become actively involved and the development of a fully competitive market. However, this may soon change, depending on the outcome of current proposals to reform Canada’s insolvency laws. Further discussion of these reform proposals is set out later in this article.

\(^1\) See United States Code, Title 11, § 361-364.
\(^3\) R.S.C. 1985, c. C-36, as amended.
While the preceding comments have addressed the question of DIP financing primarily from the perspective of independent providers of such financing (i.e. players not having an existing involvement with a borrower), financing for the distressed debtor in a restructuring or workout context may actually be available from a variety of potential sources, including the borrower’s existing lenders.

Why would an existing lender make additional advances to a troubled borrower? As discussed further below, in some cases it may be done purely for defensive purposes to protect the lender’s existing position or preclude another party from gaining a perceived advantage. In other cases, it may be done for other reasons of self-interest; for example, to avoid having to recognize an immediate loss, to gain or preserve a strategic advantage in the proceedings or to enhance the prospects of a successful restructuring (or more productive realization) over the longer term. In those comparatively rare situations where most, if not all, of the existing financing is unsecured, an existing lender may also realize an opportunity to protect its interests, possibly gain some leverage and, at the same time, generate fee and interest income to partially off-set the loss which it might otherwise suffer. Conversely, of course, in this latter scenario, the opportunities are also enhanced for new players since they may be able to offer competitive terms for new financing on a secured basis without having to invite the debate as to whether it is or is not appropriate to “prime” an existing secured lender.

There will be cases in which an existing lender (or affiliate) will see fit to make a DIP loan to secure other strategic objectives including greater control over the restructuring proceedings. The most striking recent example of this was in the Air Canada proceedings under

\[ ^3 \text{R.S.C. 1985, c. B-3, as amended.} \]
the CCAA where General Electric Capital provided a substantial DIP financing commitment to
the company. In so doing, GE was able to influence the treatment of existing loans and advances
made by an affiliate and secure a strategic seat at the table in terms of the direction and terms of
Air Canada’s overall restructuring.

Air Canada took the position that the DIP financing was essential to create
confidence in the marketplace as to the company’s ability to fulfill its commitments and
complete a successful restructuring. Air Canada also argued that there was likely no other party
who would provide a commitment of this magnitude and that the costs and other terms were
reasonable in the circumstances. However, some critics felt that the terms of the DIP financing
were not appropriate and that GE was overcompensated in relation to the financing provided.
This point of view was undoubtedly influenced by concerns over Air Canada’s management and
governance structure and the fact that there was no openly competitive process for bidding on the
DIP financing.

Several years earlier, in the initial CCAA proceedings involving the T. Eaton
Company, the company faced a situation where the borrowings from its major lenders were
unsecured. Much to the consternation of those lenders, the company set about obtaining DIP
financing from a third party lender (GE Capital) on a secured basis, without benefit of
consultation with the existing lenders. It became evident that, among other concerns held by the
lenders, there was a fundamental lack of confidence in the company’s management. In addition,
the lenders were clearly annoyed by the fact that they were deprived of the opportunity to
consider providing the DIP financing themselves, which they might well have done for either
strategic or defensive reasons.
One could make the argument that DIP loans are all about control over the debtor and its restructuring proceedings. In one sense, a DIP loan is functionally the same as a loan made to a receiver secured by a first priority charge over the assets under the terms of the appointment order. The key difference is that, in a receivership, the receiver (presumably someone in whom the lenders or other key creditors have confidence) is in control of the situation whereas in a CCAA or a BIA proposal proceeding, current management of the debtor remains in control. If an existing lender has confidence in management and its abilities to implement a successful restructuring and the debtor’s financing requirements are reasonable and consistent with a sound business plan, the lender may conclude that it is in its interest to provide funding to better secure its position or gain additional influence in the restructuring proceedings.

Conversely, a lender may decide not to provide DIP financing for a number of reasons. In some cases, the financing requirement is too large in relation to the lender’s existing exposure. Alternatively, the lender may have doubts about the integrity or capabilities of existing management or its ability to achieve its cash forecast or business plan objectives. Finally, the lender may lack confidence in its own liquidation analysis, with a resulting lack of confidence in its ability to achieve a favourable exit and recover the amount of the DIP loan should the restructuring not be successful. In this regard, it should be noted that one of the reasons that asset-based lenders have had such an impact in the marketplace is that they have expertise and years of experience in assessing collateral and structuring loans in a way to ensure that they can maximize recovery and minimize losses through an exit from the lending relationship whether in or outside of a formal restructuring proceeding.

In the CCAA proceedings initiated by Euro United Corporation, the existing lenders had indicated that they were not prepared to make further advances. The company
sought approval for DIP financing from a third party on a first secured, priming basis over the objection of the existing secured lenders. The lenders argued that their loans were under-collateralized and that they had no confidence in existing management and its financial projection. The lenders asked the Court to appoint an interim receiver. In his decision, Blair J. of the Ontario Superior Court of Justice noted that he was not satisfied that DIP lending could be authorized without serious prejudice to the secured lenders and found that it was more appropriate to appoint an interim receiver in the circumstances.4

A brief discussion of the perspectives of different players who may be a source of financing in a restructuring context follows.

A. Third Party DIP Lenders

A DIP lender who has no existing relationship with the debtor looks at a DIP loan as a new opportunity to be assessed on a stand-alone basis. The lender will typically require security, invariably on a secured or “priming” basis (where there is existing secured debt). The pricing of the loan, while it may be competitive from a DIP financing perspective, will often be set significantly above the cost of typical pre-workout financing which might have been available to the borrower. In addition, the availability of advances under the DIP financing may be limited, both in terms of the absolute amount and margining with reference to existing collateral. This is certainly not surprising since the DIP lender is looking at earning a sufficient rate of return in a relatively short time period while minimizing, to the greatest extent possible, the inherent risk in advancing new money to a troubled enterprise. With a first ranking charge

and other protections which are typically built in to a DIP order, a DIP loan can be a low risk/high return proposition in many cases.

The absence of specific rules for DIP lenders and protections for existing lenders has created uncertainty as to the test which should be applied by the Courts in authorizing DIP financing in the context of a CCAA proceeding. Without the benefit of the concept of adequate protection of the interests of existing lenders which is enshrined in the U.S. Bankruptcy Code, courts in Canada have had to establish rules and guidelines as to when DIP financing ought to be approved on an ad hoc basis. As in so many other cases involving the application of the CCAA, judges have relied on their inherent jurisdiction in order to create appropriate rules on a case by case basis, consistent with the “balancing of potential benefits and prejudices” approach which is characteristic of proceedings under the CCAA. This Canadian marketplace reality has had a significant impact on both the availability and pricing of DIP financing.

B. The Existing Lender

In view of the legal and practical restrictions on DIP financing in Canada, borrowers often have no alternative but to turn to their existing lenders for the additional financing required to support a successful restructuring or workout. From a policy perspective, this may not be a good thing since it can allow lenders to have a greater degree of control or influence over restructuring proceedings than might otherwise be warranted. No doubt, many borrowers would share this concern.

From the perspective of the existing lender, advancing additional capital may tie in to the lender’s overall objective to control the proceedings and attempt to ensure the success of the workout or, alternatively, the avoidance or minimization of losses. The additional financing
could take the form of new advances or continuation of revolving credit advances under an existing (secured) facility or a new stand-alone DIP facility advanced on a first priority or priming basis.

In some cases, financing has been provided by existing lenders primarily as a defensive strategy to avoid the risk that a new lender could enter onto the scene with the risk of priming the existing lender and either securing a strategic advantage for itself or limiting the strategic opportunities of the existing lender in the restructuring process. The pricing and terms of financing provided by an existing lender in this context might be more favourable in some cases; however, in other cases the terms may be as onerous if not more onerous than those which would be provided by an independent DIP lender due to the legal and practical barriers to DIP lending which effectively limit competitive bidding for new funding.

In certain other cases, existing lenders or their affiliates have been known to advance monies, whether by way of extensions of credit under an existing secured credit facility or by way of DIP financing, for the sole reason that the additional liquidity is likely to facilitate a liquidation or sale of the business in the circumstances where the incremental financing is expected to be repaid and the ultimate return or loss on the existing debt will hopefully be less than what it would have been had the business been shut down and the assets liquidated immediately without benefit of the continued operations made possible through the new advances.

This type of advance is analogous to the receivership lending scenario referenced above where the lender provides the necessary liquidity on a first secured basis under the protection of a court order to enable a receiver to liquidate assets or to continue operations while
attempting to realize higher returns through a sale on a going concern basis. In recent years, a
trend has developed whereby these efforts have frequently been undertaken under the aegis of a
CCAA proceeding, either with or without a plan of arrangement, rather than through a
receivership proceeding.\(^5\)

C. Other Participants in the Distressed Debt Market

There are other potential sources of financing or capital which can also come into
play in a restructuring or workout context. For example, in many situations, existing
subordinated lenders or equity participants may be prepared to advance additional funds;
however, in sharp contrast to DIP financing or additional financing provided by an existing
(secured) lender, these types of advances are highly speculative and the pricing will invariably
reflect the higher degree of risk which is being undertaken. In some cases, the parties providing
financing of this nature are doing so as part of a broader strategy related to the borrower; for
example, a desire to acquire equity or voting control in the context of a restructuring. In other
cases, financing of this nature may be provided as an adjunct or condition precedent to securing a
DIP financing or a commitment for additional financing from an existing lender.

\(^5\) Consider, for example, the following CCAA proceedings in which companies have been sold or liquidated, often without
a plan of arrangement ever being filed:

- Nevada Bob’s Golf Inc. (2000)
- American Eco Corporation (2000)
- Consumers Packaging Inc. (2001)
- Fantom Technologies Inc. (2001)
- Veltri Metal Products Co. (2004)

The Nevada Bob’s filing was in Alberta; all of the other cases mentioned occurred in Ontario. In the Fantom case, there
was the concurrent appointment of an interim receiver. In the Irwin Toy case, an interim receiver was appointed some six
weeks into the CCAA proceedings, which continued and ultimately resulted in the successful implementation of a plan of
arrangement.
There are also institutional or private financiers (so-called lenders of last resort) with capital available for investment in high-risk restructuring situations. As noted above, in some cases, such an investment may be made as part of a strategy to support an acquisition of the equity of a troubled company with a view to taking control, either with a longer term strategic objective (buy and hold) or with the view to achieving an investment return over the medium to long term, premised on the completion of a successful financing and/or operational restructuring leading to either repayment or a possible sale of the investment itself.

In recent years, we have witnessed the development of an active marketplace for the purchase and sale of corporate debt, including bonds, trade debt, subordinated and even senior debt, where the purchaser’s objective from the outset may be to acquire control over a restructuring proceeding. For example, where a purchaser is able to acquire sufficient debt to a point where it may be able to influence or, alternatively, veto a vote on a restructuring proposal or plan of arrangement, the investor may proceed with a view to implementing that strategy but with the knowledge that, even if that strategy is not successful, the purchaser may preserve the opportunity for a profitable exit, generating gains through trading up on the value of the debt or equity which has been acquired.

Alternatively, in other situations where the restructuring plan will likely contemplate the conversion of existing debt to equity, the purchaser of distressed debt may proceed on the assumption that it can ultimately gain effective control over the equity of the restructured entity which, if successful, will generate investment returns and/or opportunities for gains on the sale of the investment, recognizing that the original debt was purchased at a discount to par value. To a certain degree, this objective can be seen as being inconsistent with the objectives of some existing stakeholders, including the debtor’s management. However,
since governance is often a primary concern in a restructuring, it could be argued that other stakeholders’ interests may actually be better served by the intervention of a financier or investor with objectives which are fundamentally different from those of current management or stakeholders.

**The Future and Potential Impact of Insolvency Reform**

The landscape for corporate lending in Canada has changed dramatically over the past several years. Canadian banks, who have long dominated the marketplace, have significantly reduced their traditional lending activity after being battered in the last recession, in favour of more lucrative returns available in other areas. The resulting void has been filled by new players, including asset-based lenders who employ a different approach to lending and a different philosophy in managing their portfolios.

There is no reason to believe that these trends will be reversed in the near future. Accordingly, borrowers and other stakeholders such as trade creditors will have to continue to adapt to this evolving reality.

One factor which could help to shape these trends or otherwise influence future developments in this area is the potential reform of Canada’s insolvency laws. A five year review of Canada’s insolvency laws was mandated after the last round of relatively modest reforms enacted in 1997 and is now overdue. It remains to be seen whether significant reforms will be enacted in the near future.

In its report to Industry Canada in March 2002, the Joint Task Force of the Insolvency Institute of Canada and Canadian Association of Insolvency and Restructuring
Professionals (the “JTF”) made a number of important recommendations on insolvency law reform, including in the area of DIP financing.\(^6\) The JTF observed that, while the CCAA is silent on the subject, Canadian courts have decided that they have the inherent jurisdiction to authorize DIP financing but that there continues to be a debate regarding the court’s jurisdiction and the basis upon which that jurisdiction should be exercised.\(^7\) The JTF noted the importance of DIP financing in an insolvency system intended to promote restructuring rather than liquidation and going concern solutions which would maximize the value for all stakeholders.

The JTF therefore proposed that there should be codification of certain principles including various factors which the court should consider in deciding whether or not to authorize DIP financing. Among the criteria which the JTF recommended should be considered were the following factors\(^8\):

- \(a\) what arrangements have been made for the governance of the debtor during the proceedings;
- \(b\) whether management is trustworthy and competent and has the confidence of significant creditors;
- \(c\) how long will it take to determine whether there is a going concern solution, either through a reorganization or a sale, that creates more value than a liquidation;
- \(d\) whether the DIP loan will enhance the prospects for a going concern solution or rehabilitation;
- \(e\) the nature and value of the assets of the debtor;
- \(f\) whether any creditors will be materially prejudiced during that period as a result of the continued operations of the debtor; and

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\(^6\) The Insolvency Institute of Canada and Canadian Association of Insolvency and Restructuring Professionals, Report of the Joint Task Force on Business Insolvency Law Reform (“JTF Report”), March 2002

\(^7\) JTF Report commentary at p. 27

\(^8\) Ibid. at pp. 15 and 29
(g) whether the debtor has provided a detailed cash flow for at least the next 120 days.

It is most interesting to note that the issue of governance appears first on the JTF’s recommended criteria.

The report of the Standing Senate Committee on Banking, Trade and Commerce on the review of the BIA and CCAA included specific recommendations on DIP financing.9 In its report, the Senate Committee adopted certain recommendations made by the JTF, recommending that Canada’s insolvency statutes be amended to permit DIP financing. In determining whether or not to authorize DIP financing, the Senate Committee recommended that the court should be required to consider the factors outlined in the JTF report.

Whether these recommendations are ultimately enacted remains to be seen. If they are, it should remove some of the uncertainty which currently has the effect of limiting the number of players and the opportunity to create a competitive marketplace in the DIP financing area. The development of such a market could have a significant impact on the course of restructuring and work out proceedings in Canada and bring Canada’s insolvency laws more closely in line with those of its largest trading partner.

**Conclusion**

Restructuring proceedings will continue to evolve in Canada as the market for distressed debt lending matures and the number of players who are actively involved in the marketplace continues to increase. The reform of Canada’s insolvency laws, including the enactment of specific provisions relating to DIP financing, will likely enhance that development

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9 Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies’ Creditors Arrangement Act; Report of the Senate Committee on Banking, Trade and Commerce, November 2003
and produce positive results for debtors as well as other stakeholders involved in corporate restructurings and loan workouts. A system which creates more latitude for the restructuring debtor and its creditors (coupled with necessary changes to address governance issues) is likely to promote restructurings ahead of liquidations. This would be a positive development to the extent that it promotes enhanced recoveries and better results for all stakeholders while, at the same time, helping to reduce some of the social costs and other consequences resulting from failed restructurings.

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