

## restructuring bulletin

July 2008

### *Wage Earner Protection Program Act and certain other amendments to the BIA now in force*

On July 7, 2008 specific provisions of the *Insolvency Reform Act, 2005* and the *Insolvency Reform Act, 2007* were proclaimed into force by Order in Council. As a result, the *Wage Earner Protection Program Act* (the “WEPPA”) and certain related amendments to the *Bankruptcy and Insolvency Act* (“BIA”) have come into immediate effect.

Certain of those amendments are intended to protect current and former employees of insolvent companies and will affect lenders to insolvent businesses.

Under the WEPPA, an employee whose employer has become bankrupt or subject to receivership on or after July 7, 2008 is entitled to receive payments from a federal Wage Earner Protection Program on account of any outstanding wages that were earned in the six months immediately prior to bankruptcy or the first day of receivership in an amount not to exceed the greater of \$3,000 and four times the maximum weekly insurable earnings under the *Employment Insurance Act*.

### wages and vacation pay lien

Corresponding amendments to the BIA are now in force that provide an employee of an employer which is bankrupt or in receivership, with a priority charge on the employer’s “current assets” for unpaid wages and vacation pay (but not for severance or termination pay). This charge will secure unpaid wages and vacation pay for the six month period prior to bankruptcy or receivership to a maximum of \$2,000 per employee (plus up to \$1,000 for expenses for “traveling salespersons”). The priority charge ranks ahead of all other claims except unpaid supplier rights.

Under the law as it stood prior to these amendments coming into force, in a bankruptcy, wages and vacation pay were subordinate in priority to secured creditors’ claims. However, in practice, secured creditors would often agree to cover payroll arrears for a variety of practical reasons in insolvency proceedings, including the need to secure employee cooperation and because of the personal liability faced by directors of insolvent companies. The practice with respect to vacation pay is more variable; while vacation pay claims would not have priority in the context of a bankruptcy, payments are sometimes made to secure cooperation of the employees or due to potential personal liability on the part of the directors.

Accordingly, as a practical matter, many asset-based lenders lending on the security of operating assets (inventory and receivables) will already account

for these types of claims as potential reserves in borrowing base calculations. Lenders will have to assess whether or not the new statutory priority for wage and vacation pay arrears merits any changes to their current reserve practices.

## pension contributions lien

The BIA now also grants a priority charge in bankruptcies and receiverships for outstanding current service pension plan contributions, ranking behind the employee remuneration priority but otherwise with the same priority as is accorded to that lien. The pension contribution priority extends to all assets, not just current assets, and is unlimited in amount.

The charge secures (1) amounts deducted as pension contributions from employee wages but not contributed to the plan prior to a bankruptcy or receivership and (2) amounts required to be contributed by the employer to a pension plan, for “normal costs”. The priority does not extend to unfunded deficits arising upon a windup of a defined benefit plan and should not include scheduled catch-up or special payments required to be made by an employer because of the existence of a solvency deficiency.

The existence of this lien underscores the importance of effective reporting and monitoring of pension contributions by the borrower, as well as other employee obligations such as vacation pay.

## other amendments now in force

Other amendments proclaimed into force include those relating to the implementation of the Cape Town Convention and the Protocol on Matters Specific to Aircraft Equipment, exemptions for RRSP and RIF property, and the discharge of debts or liabilities resulting from property or services obtained through false pretences or fraudulent misrepresentation.

The balance of the other significant amendments to the *Bankruptcy and Insolvency Act* and *Companies' Creditors Arrangement Act* have not yet been proclaimed into force and are expected to be proclaimed later this year.

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## a cautionary note

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