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PRACTICAL, DEFENSIVE MOVES IN UNCERTAIN ECONOMIC TIMES

Jaclyne Reive – Louis Amato-Gauci – Bobby Sachdeva – Manjit Singh

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It's Time to Review your Agreements!

Insolvency and Restructuring: Key Considerations for the Transport and Logistics Industry

Government Relief Programs and Related Tax Issues



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It's Time to Review your Customer and Service Provider Agreements!

Jaclyne Reive and Louis Amato-Gauci

Have Your Operational Procedures Changed?

- Consider each operational step in your business process.
- What changed in each step as a result of COVID-19?
- What was the impact of each change on the business?
- Which changes should continue as businesses re-open?

How Does Your Contract Compare?

- Review how procedures are described in your customer and service provider contracts.
- Are new procedures different than what the contract requires?
- What sections will need amendments due to operational changes?
- Don't forget to look at the big picture too!

Payment and Financial Positions

- Consider the financial position of your service providers and customers.
- Do you have a right to demand financial information or other assurances?
- What steps are you allowed to take to ensure receipt of payments?
- Interest Rates?
- What about subcontracted services?

Lien and Set-Off Rights

- Does the contract allow for lien rights or a waiver?
- Is it a general or specific lien?
- What is the lien process / steps to assert a lien, based on the contract?
- Every contract may have different rules.
- Does the contract allow for set-off rights?
- How does set-off impact you?

Review Completed, Now What?

- Now that you have considered:
 - what has changed
 - how you can make sure you receive payment
 - what contractual rights you can rely on
- Determine where contract provision changes are needed.
- Start negotiating those changes!

Force Majeure

“A contractual term by which one (or both) of the parties is entitled to cancel the contract or is excused from performance [...] or is entitled to suspend performance [...] upon the happening of a specified event or events beyond [their] control.”

HG Beale, ed. *Chitty on Contracts*, 30th ed.



Components of Force Majeure

1. One party, typically the supplier or service provider, declares an event of force majeure
2. That party is excused from supplying the goods or services, and counterparty is excused from buying the goods or services, while performance is suspended
3. Typically there are duties to mitigate
4. After defined period of time, either party can exit the contract, bringing the relationship to an end

Atlantic Paper Stock Ltd. v. St. Anne-Nackawich Pulp and Paper Company Limited, SCC (1976)

1. Force majeure must meet two conditions:
2. It must clearly be beyond the control of the contracting parties
3. The event must render performance of the obligations impossible
4. Mere commercial hardship is not sufficient.

Thames Valley Power Ltd. v Total Gas & Power Ltd., [2006] 1 Lloyd's Rep 441

“... It does not at all follow that the supplier is entitled to rely upon an increase in the market price in comparison to the contract price as a *force majeure* circumstance. ... This conclusion is consistent with a line of cases, both on *force majeure* clauses and on frustration, ... to the effect that the fact that a contract has become expensive to perform, even dramatically more expensive, is not a ground to relieve a party on the grounds of *force majeure* or frustration.”

Alternatives: The ICC Hardship Clause

“...where a party to a contract proves that: [a] the continued performance of its contractual duties has become excessively onerous due to an event beyond its reasonable control which it *could not reasonably have been expected* to have taken into account at the time of the conclusion of the contract; and that [b] it *could not reasonably have avoided or overcome* the event or its consequences, the parties are bound, within a reasonable time of the invocation of this Clause, to negotiate alternative contractual terms which reasonably allow for the consequences of the event.”

Alternatives: Price Adjustment Clause

- Fees payable under the contract are subject to adjustment
- Specify whether the fees are guaranteed during initial period
- Identify events may trigger an upward/downward adjustment
- Ideally, link adjustment calculations to recognized index
- Specify how often adjustments will occur
- Buyer may want right to audit / verify proposed adjustments

When the Other Party Claims Force Majeure

- Review the contract: does it have a force majeure clause?
- What is the governing law and choice of venue for disputes?
- Does the event qualify as force majeure?
- What are the consequences of non-performance?
- Require the party claiming force majeure to provide:
 - details of all relevant circumstances
 - details of all efforts to resume performance or mitigate
- Try to negotiate a commercially sensible amendment

Don't Wait for a Notice of Force Majeure

- Get ahead of the issue
- Review all material contracts
- Contact your counterparties and see how things are going
- Be sensitive to current circumstances
- Discuss (without prejudice) how terms might be amended
- Keep in mind:
 - the duty of good faith in contract performance; and
 - you may need to claim force majeure in the future



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Insolvency and Restructuring

Bobby Sachdeva

Overview of Insolvency Considerations

3 Different Looks at the World of Insolvency & Restructuring

1. Available Insolvency remedies if your business needs to restructure
 - What are the differences between the major insolvency structures available in Canada?
2. How to protect yourself when doing business with companies going through insolvency proceedings
 - The risks inherent in debtor driven insolvency proceedings and measures available to protect your financial interests
3. Current Crisis: Mitigating Risks and Seizing Opportunities

Canada Has Four Key Insolvency Statutes

- *Companies' Creditors Arrangement Act (CCAA)*
 - *The Bankruptcy and Insolvency Act (BIA)*
 - *Personal Property Security Act (PPSA)*
 - *Provincial Rules of Court (Courts of Justice Act)*
-
- The last two are not insolvency legislation but play into a lot of insolvency remedies and procedures.

Common Elements of Insolvency Proceedings

- Stay of proceedings (by order or statute) which includes a “freeze” of litigation proceedings and enforcement rights
- Appointment of Court Officer (CCAA – Monitor; BIA – Receiver or Trustee)
- Claims process (BIA proposal or CCAA proceedings)
- Contracts or agreements with debtor company can be disclaimed

Companies' Creditors Arrangement Act (“CCAA”)

- Federal statute for the reorganization of a large insolvent corporation or group of companies
- Available where company or the affiliated group of companies have more than C\$5 million of claims in the aggregate
- Analogous to Chapter 11 of the U.S. Bankruptcy Code
- Flexible statute
- Permits company/companies to file a plan of restructuring and compromise for its creditors with a view to keeping the debtor company operating, increasing the amount that may ultimately be paid to creditors and preserving the debtor's employees' jobs, etc. (Air Canada 1.0, Stelco)
- Can also be a liquidation or wind up (Target)

Bankruptcy and Insolvency Act (“BIA”)

- Also a federal statute that includes provisions to facilitate both the liquidation and reorganization of insolvent debtors.
- **Liquidation provisions**: provide for the appointment of a licensed insolvency trustee (LIT) (formerly known as a trustee in bankruptcy) over the assets of the insolvent debtor [analogous to Chapter 7 of the U.S. Bankruptcy Code]
- Bankruptcies are a creditor driven process. The Trustee takes instructions from an elected committee of creditors known as Inspectors.
- Companies almost never come out of bankruptcies.
- Trustee’s job is marshal the bankrupt’s assets, sell and realize on those assets and then distribute funds to the unsecured creditors who have provable claims in the bankruptcy by way of dividends (after secured creditors are addressed)
- **Proposals**: The reorganization provisions under the BIA are more commonly used for smaller, less complicated reorganizations than those that take place under the CCAA because the BIA proposal provisions have more stringent timelines and provide less flexibility than the CCAA

The BIA (cont'd)

- Debtor often continues to operate. Can be a restructuring or organized sale.
- Used to shed debt and continue with business. Often sees new money come into the business or the sell off of portions of the business.
- Early planning is essential given tight time lines. Initial 30-day stay with up to three 45-day extensions.
- Approval of creditors: 51% of voting creditors in number and $\frac{2}{3}$ of dollar value of debt (of voting creditors)
- Court approval required as well.
- **Receivership**: Court ordered appointment of court-officer to take control of and realize upon assets and property of debtor under Section 243 of BIA. Debtor is done. Most often formal insolvency mechanism utilized by secured creditors.

Not to be Forgotten- OBCA / CBCA and PPSA

OBCA

- While not an insolvency statute, OBCA / CBCA contain broad powers under oppression remedy provisions [s. 248]
- Where Court determines that there has been oppressive conduct, unfairly prejudicial conduct, or conduct that disregards the interests of any shareholder it may make an order to resolve the matter in a variety of ways, including appointing a receiver or setting aside a transaction
- Court can also order that corporation be wound up and appoint a liquidator to wind up business and affairs and distribute property
- Often used in the Context of Shareholder Disputes

Not to be Forgotten- OBCA / CBCA and PPSA (cont'd)

PPSA

- Perfection of security interests and priorities of secured creditors.
- Rights of secured creditors and rules for realization on collateral subject to security
- Security provides a wide array of options and remedies not available to unsecured creditors (think shareholder loans)
- Foreclosure

Debtor Driven Insolvencies: CCAA and Proposals Under the BIA

KEY TAKE AWAY - YOU ARE STILL DOING BUSINESS WITH THE DEBTOR

- **Proposals Under the BIA** – Proposal Trustee monitors the Debtor's business and actions and ultimately reports to the Creditors and the Court. However, in most instances the Proposal Trustee has no control over the Debtor's receipts and disbursements and is not a backstop to make sure the invoices of those doing business with the Debtor will get paid.

Debtor Driven Insolvencies: CCAA and Proposals Under the BIA (cont'd)

- **CCAA** – The Court appointed Monitor often more involved but is not responsible for ensuring that ongoing payments are made. But more room for negotiation and flexibility of Court Orders to ensure payment priorities to suppliers during the process. Also the Critical Supplier provisions under the CCAA (Section 11.4). Order can be obtained declaring a supplier to be a “critical supplier”. Double edged sword. Ongoing obligation to supply on terms set by the Court but there can be security for payment built into the Order.
- **Receivers and Trustees** – Usually direct contract and payment not a concern

Risks and Opportunities

- Financial Difficulties
 - early planning
 - shed expenditures
 - search for new lenders or equity infusion
 - be realistic (sometimes “going all in” is not the right move and an organized wind down is the best option)
 - seek advice before it becomes urgent
- Opportunities
 - acquisitions, consolidation, investment opportunities and growth



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Government Relief Programs and related tax issues

Manjit Singh



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Tax Considerations Related to Insolvency

Debt Forgiveness Rules, Foreclosures and Seizures

Debt Forgiveness Rules

- Generally, debt forgiveness rules (section 80) apply when
 - there is a settlement or extinguishment of a debt
 - the FMV of the consideration on settlement is less than the tax cost (i.e., principal amount) of the debt
- Once a debt forgiveness is established, the “forgiven amount” is applied on a cascading basis to grind down tax attributes of the borrower

Debt Forgiveness Rules (cont'd)

- The forgiven amount is applied automatically to reduce in the following order:
 - non-capital losses (net of allowable business investment losses)
 - farm losses
 - restricted farm losses
 - allowable business investment losses
 - net capital losses

Debt Forgiveness Rules (cont'd)

- Applied at the borrower's discretion (on election) among UCC of depreciable property (and, if applicable, various categories of resource expenditures)
- Reduces ACB of certain capital property (i.e., portfolio investments, land)
- Reduces ACB of certain shares and debts of corporations (i.e., of a company of which the borrower owns more than 10% equity)
- Reduces current-year capital losses (if greater than current-year capital gains)
- If remaining balance, 50 percent included in income (100% inclusion if borrower is a partnership)

Foreclosure and Seizure Rules

- Different tax rules apply to debtors and creditors where there is a seizure of property due to debtor's failure to pay debt owed to creditor
- Rules apply to foreclosures and conditional sale repossessions

Rules Applicable to Debtors (Section 79)

- Generally, debtor deemed to dispose of property for proceeds equal to the unpaid principal and interest
- If more than one property is surrendered at the same time, the deemed proceeds are prorated based on relative FMV of properties
- Debt forgiveness rules generally do not apply where these rules apply

Foreclosure and Seizure Rules (cont'd)

Rules Applicable to Creditors (section 79.1)

- Generally, the creditor deemed to have acquired the seized property at a cost equal to the creditor's cost of the debt obligation, subject to certain adjustments
- Where more than one property is seized at the same time, the deemed cost is prorated based on the relative FMV of properties
- Creditor deemed to have disposed of the debt obligation for proceeds equal to its adjusted cost base (so no gain or loss realized on the debt)
- Any subsequent payment of the debt generally results in a capital gain to the creditor



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Covid-19 Relief Measures For Businesses

Recent Updates

Canada Employer Wage Subsidy (CEWS) – May 15, 2020 Updates

- Provides eligible employers with 75% of weekly remuneration paid to employees, up to weekly max. of \$847, retroactive to March 15, 2020
- CEWS has been extended to August 29, 2020
- Regulations to the Act were approved to extend the eligibility of the CEWS to certain groups, including:
 - Partnerships that are up to 50-per-cent owned by non-eligible members
 - Indigenous government-owned businesses
 - Non-public colleges and schools (e.g. driving schools; flight schools)

(CEWS) – Expected Legislative Amendments

- Expanding “eligible entities” to include corporations formed on amalgamations, by permitting benchmark revenue to be computed using combined revenues;
- Trusts with employees would continue to be eligible for the CEWS, subject to the following new exceptions (applied prospectively):
 - Where trust is a tax-exempt entity (other than a public institution), it qualifies only if it is a registered charity or one of the other types of eligible tax-exempt entities; and
 - Where the trust is a public institution, it would qualify only if it is prescribed by regulation

(CEWS) – Expected Legislative Amendments (cont'd)

- Consultation with key business and labour representatives underway on potential adjustments to CEWS, including the 30 per cent revenue decline threshold, to maximize employment support and post-crisis recovery;
- Not yet known how qualifying revenues for the extended periods (June, July, August) will be measured;
- Amendment to allow employers to choose (on employee by employee basis) one of two periods when calculating the baseline remuneration of their employees:
 - as the average weekly remuneration paid to the employee from January 1 to March 15 of 2020 or
 - as the average weekly remuneration paid to the employee from March 1 to May 31 of 2019
 - in both cases excluding any period of 7 or more consecutive days without remuneration
 - Change is proposed to be retroactive to April 11, 2020

Tax Relief for International Tax Issues Due to COVID-19 Travel Restrictions

- CRA concessions announced on May 19, 2020 respect to international tax issues arising due to Covid-19 Travel Restrictions
- Concessions apply from March 16 until June 29, 2020, unless extended

183 Sojourning Rule - Individuals

- Days of physical presence in Canada solely because of the Travel Restrictions will not count towards an individual's residency in Canada under the 183-day sojourning rule or the "common law" residency test, assuming a return to the country of residence when able

Corporate Governance

- Foreign corporations will not be considered to become resident in Canada if a director of a corporation must participate in a board meeting from Canada because of the Travel Restrictions (i.e. central management and control will not be found to be in Canada)
- Similar application for commercial trusts

Tax Relief for International Tax Issues Due to COVID-19 Travel Restrictions (cont'd)

Carrying on Business / Permanent Establishment in Canada

- PE not considered to be established in Canada only because employees perform their duties in Canada solely as a result of the Travel Restrictions,
- Not considered to have an "agency" PE solely due to a dependent agent concluding contracts in Canada where such activities would not have been performed in Canada but for the Travel Restrictions
- Any days of physical presence in Canada due solely to Travel Restrictions will not count towards the 183-day presence test in "services PE" provision
- If a non-resident of a non-treaty country can demonstrate that it has crossed the threshold of carrying on business in Canada only because of the Travel Restrictions, CRA "will consider whether administrative relief is appropriate on a case-by-case basis."

Tax Relief for International Tax Issues Due to COVID-19 Travel Restrictions (cont'd)

Cross-Border Employment Income

- U.S. residents who exercise their employment in Canada solely as a result of the Travel Restrictions will not have those days count towards the 183 days exemption in Canada-US treaty (Art. XV(2))
- Reg. 105 or 102 waiver processing delays. CRA will not assess for failure to have withheld if the sole reason for not obtaining the waiver was Covid 19 related and employer demonstrates having “taken reasonable steps to ascertain that the non-resident person was entitled to a reduction or elimination of Canadian withholding tax by virtue of an income tax treaty with Canada”

Section 116 Certificates

- Processing of s. 116 certificate requests was interrupted and processing has only resumed with a “limited capacity”
- “urgent requests for comfort letters may be submitted on a temporary basis”

Large Employer Emergency Financing Facility - LEEFF

- Announced on May 13, 2020, LEEFF provides short-term liquidity assistance in the form of interest-bearing term loans to large Canadian employers until they can access more traditional market financing.
- Eligibility - large Canadian employers including NPOs, other than those in the financial sector, that have:
 - Significant operations or workforce in Canada
 - \$300 million or more in annual revenues
 - Require a minimum loan size of \$60 million
 - Committed to a sustainable business plan
- Size/Principal Amount – minimum \$60 million
 - 80% as an unsecured facility
 - 20% as secured facility
 - To be advanced in tranches over 12 months

Large Employer Emergency Financing Facility – LEEFF (cont'd)

- Interest Rate
 - **Unsecured Facility:**
 - i. Year One - 5% rate per annum, payable quarterly in arrears
 - ii. Year Two - 8% per annum
 - iii. Subsequent Years - increase each year by a further 2% per annum
 - iv. Interest may be paid in-kind for the first two years of the loan
 - **Secured facility: based on interest rate of the borrower's existing secured debt**
 - i. Term
 - ii. Five year term on the unsecured facility
 - iii. Secured loan facility to match term of borrower's existing secured debt
 - iv. Ability to prepay without penalty

Large Employer Emergency Financing Facility – LEEFF (cont'd)

- **Restrictions** - The borrower will be subject to certain operating requirements while the loan is outstanding including, (i) prohibitions on dividends, capital distributions and share repurchases, and (ii) certain executive compensation restrictions.
- **Covenants** - The borrower to affirm certain covenants while the loan is outstanding including,
 - i. performance of obligations under existing pension plans;
 - ii. performance of material obligations under applicable collective bargaining agreements; and
 - iii. support climate control initiative (publishing an annual climate-related financial disclosure report, highlighting corporate governance, strategies, policies and practices to manage climate-related risks and opportunities and contribute to achieving Canada's commitments under the Paris Agreement and goal of net zero by 2050).
- **Governance** - Canada Enterprise Emergency Funding Corporation (CEEFC) to have right to appoint an observer to the board of the borrower
- **Conditions** - Include certain waivers from existing lenders or bondholders of the borrower



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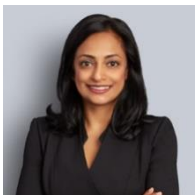
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