

*Empirical Analysis of the Effectiveness of Reorganization
Procedures under the BIA and the CCAA*

**STUDY CONDUCTED FOR
THE OFFICE OF THE SUPERINTENDENT OF BANKRUPTCY**

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The authors are responsible for any errors of observation or interpretation that may be found in this report.

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INTRODUCTION

Background

Managing a company can be defined as adapting it to a changing environment. The company may experience difficulties with adaptation that are temporary, or more profound. Commercial insolvency arises when adaptation has become so difficult that management's autonomy in managing the company is threatened. Canadian legislation in the area of commercial insolvency comprises two Acts: the *Bankruptcy and Insolvency Act* (BIA) and the *Companies' Creditors Arrangement Act*.

Levels of commercial insolvency, in terms of the number of companies having recourse to liquidation or reorganization procedures under the BIA, have increased significantly over the last decades, with an average annual rate of growth of a little over 4% for the period 1966-2001. This trend has reversed in the last few years insofar as the total number of cases. But of this total number of companies, the number of those availing themselves of reorganization procedures under the BIA (as amended in 1992) has increased at an average annual rate of 14% since 1993. The depth of commercial insolvency, in terms of the liability ratios of insolvent businesses, which can be qualified as their degree of insolvency, has been experiencing a strong upward trend that began in the late 90s. The data on total net liabilities of companies which recently became insolvent under the BIA provide a good illustration of this trend in degree of insolvency. Hovering around an average of \$2 billion in the late 80s, and around \$4 billion in the 90s, total net liabilities increased to \$8 billion between 1999 and 2002.

Levels of commercial insolvency, in terms of the number of companies or total commercial liability under CCAA reorganization procedures, have increased appreciably over the last two decades. Although the CCAA was introduced in 1933, it was only in the mid-80s that its use became widespread. There is an ongoing federal project to inventory the number of reorganizations executed pursuant to CCAA procedures. According to unpublished preliminary data prepared by Industry Canada's Corporate and Insolvency Law Policy Branch in 2003, approximately one hundred companies, with average assets in the order of \$300 million, took advantage of the CCAA over the period 1998-2001. There was significant dispersion around this average, with some companies reporting total assets under \$10 million, and others reporting total assets in the billions of dollars.

Businesses and insolvency

A business can be viewed as the mechanism that matches the resources of the economy with the needs of consumers. This matching can be accomplished through the physical transformation of resources, as done by businesses in the primary and secondary sectors, or by moving resources and products in time and space, as is the case with the service sector. Satisfying the needs of consumers is the end result of the company's activities. Given that the value of the company's products and its revenues flow from this satisfaction, the company is synonymous with credit. This credit, or confidence, enables management to mobilize resources. Insolvency threatens the relationship of confidence between, on the one hand, the company's management, and on the other hand, the other parties involved with the company, such as suppliers, bankers, employees or investors.

The origins of commercial insolvency are many. Insolvency may result from events external to the business that are totally out of the control of its management; events that are sufficiently unforeseeable that the absence of measures to prevent them does not reflect upon management's competence. On the other hand, they may be events that are specific to the business, over which management has a great deal of control and the means to foresee. Between these two extremes is a continuum containing an infinite number of possibilities.

The SARS epidemic, combined with the events of September 11, had a catastrophic effect on the financial situation of a good number of large air transport companies, particularly in North America. Because of the extenuating circumstances, their financial situation, which would normally be considered characteristic of insolvency, did not pose a serious threat to the relationship of trust between management and the other parties involved. Litigation that arose during the turnaround period for these companies essentially focused on issues of fairness in sharing the adjustment costs. But generally speaking, commercial insolvency arises in a grey area between the two previously identified extremes, which fact serves to call into question, at least temporarily, the competence and sometimes even the honesty of management, as well as the appropriateness of adjustments that permit the business to continue.

Reorganization procedures, effectiveness, governance and information

Legal reorganization procedures create an exception regime in that they enable management to temporarily shelter the company's assets from the remedies provided for in the original contracts associating the creditors with the company. The procedures may also allow for the termination of enforceable contracts; this option adds to the exception character of the procedures. By writing off part of its debts and terminating costly contracts, the reorganized company can once again become profitable. For some observers, or for creditors, the reorganization procedure may appear to be an easy solution that could lead to abuse. This raises the question of the appropriate, or effective, use of reorganization procedures.

Company managers have a great deal of information about the company and its daily operations. Their cooperation is preferable, even essential, for turning around an insolvent business. Reorganization procedures are not intended to criticize managers, who should have the right to make mistakes and to learn in dealing with constantly evolving situations. Rather, the objective of the procedures should be to determine as quickly as possible whether the company has the potential to be turned around and to make this happen at the lowest possible cost, while it still has access to the resources that are specific to it and that could allow for creating value.

It is not enough to simply link reorganization procedures to an objective, however laudable it may be. The definition of objectives follows logical results, while justification should refer firstly to a context that identifies the other possible means, and secondly to a framework of analysis that, through the identification of each possibility, supports the choice of the recommended means.

Technicians and engineers may view the nature of the company from the standpoint of its physical essence. For the manager, the accountant or the lawyer acting as trustee, the nature of the company is something completely different: it is a place of social interactions, a flow of transactions among the various interacting parties, a network of implicit and more formal contracts setting out guidelines in terms of the duties and conduct of each party in this trade context. Laws affect companies' activities through their impact on these transactions and contracts. In addition to the direct costs of production, for example, energy and raw materials, there are all the other costs associated with organizing transactions, managing or adjusting daily operations, supervision and negotiation.

Generally speaking, laws governing economic activity can be justified when they enable people to interact at a lower cost in a production context. When that happens, laws and the judicial system provide for greater well-being using identical resources and effort. An initial brief and superficial justification for legal reorganization procedures is represented by the contention that it would be too expensive, directly or in terms of incentives, to negotiate and draft contracts that provide for the circumstances of insolvency and that establish in advance a mechanism for reviewing contractual clauses and decreasing indebtedness under certain of those circumstances.

Regardless of the economic system, adjustment is the main challenge for business, and is a constant threat to the survival of economic organizations. While recent literature on governance stresses the importance of the relationship between shareholders and management, the theory of governance is much broader in scope¹. In general terms, it involves the study of contractual relationships whose continuity in time is a source of value². We can speak of the governance of companies as well as the governance of relationships between companies and their external partners. A good number of the contractual relationships that incorporate businesses are of this nature, and legal reorganization procedures help establish governance for companies confronted by adjustments significant enough to cause insolvency. This governance extends beyond the traditional boundaries of business governance.

In real terms, the relationships of governance are translated, among other things, by messages from a more informed party (management) to other less-informed parties (the other parties involved with the company). To a large extent, these messages consist of financial and accounting information. In order to ensure that the exception regime to which the legal reorganization procedures provide access is used appropriately, the legislator entrenched the governance issues raised by the procedures: the dissemination of financial and accounting information is a recurring requirement in the application of the procedures. For example, the BIA procedure requires that a cash-flow statement be filed within a short time of procedures being initiated. Both the BIA and the CCAA procedure also require that the trustee or monitor prepare a report on the affairs and finances of the debtor company so that the creditors can make an informed decision as to the reorganization plan being proposed.

Without crossing the line into providing misleading financial information, the accountant can sometimes choose one accounting method from among several within generally accepted accounting principles. The literature will take into account how accounting results are managed when this choice affects the data that are produced. An effective procedure will include measures and incentives that tend to limit any bias that might flow from such management of accounting results.

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1. The article by R. Gilson and M. Roe, "Understanding the Japanese Keiretsu: Overlaps between Corporate Governance and Industrial Organization" in *Yale Law Journal*, (1993, 102) demonstrates this broader scope of the governance theory.
 2. Definition produced by O. Williamson, guest speaker at the "Richard T. Ely" conference at the 2005 Annual General Meeting of the American Economic Association ("The Economics of Governance", *American Economic Review*, Papers and Proceedings, May 2005, 1-18).

Selection of cases and report plan

The first section of this report draws together a number of points of reference for analyzing the effectiveness of legal reorganization procedures from a governance perspective. The second part focuses on the use of the reorganization procedures provided for in the BIA. Close to 3,000 incorporated businesses in the Province of Quebec availed themselves of these procedures between 1998 and 2003. The research began with a detailed study tracking the progress of these businesses through the procedure and the application of the control mechanisms provided for in the Act. For purposes of comparison by sector and by whether the companies were attached to the Montréal or Québec City office, an average indicator of degree of advancement was defined and calculated for the total population and for a variety of sub-groups of companies. The results of this global research are presented in the first appendix to this report (Appendix A).

The global research served as a reference for evaluating the representativeness of samples of businesses used for the case studies. Initially, manufacturing companies that reported assets of \$1 million or more when the procedures began were selected for the preliminary case studies. The total population of close to 3,000 companies includes twenty-eight companies with these characteristics. It turned out that this sampling of companies was not very representative of the total population in terms of progress made in the procedures, because it has a higher average indicator of degree of advancement. In addition, despite their size, a good number of these companies are private companies, and there is little information available about them prior to or after their recourse to the procedure. Given the importance of financial and accounting information for this analysis, and given their lack of representativeness, these companies were not selected for the detailed case studies. After that, a listing was made of public companies in the population.

Twenty-two public companies, accounting for less than 1% of the total population of incorporated businesses, made use of a BIA reorganization procedure in the period 1998-2003. The regulations governing access to financial markets hold these companies to greater transparency, or at least to disseminating more financial and accounting information, than private companies. Given the importance accorded to the availability of financial and accounting information to ensure effective use of reorganization procedures, it seemed reasonable to assume that these public companies would lend themselves to an assessment of the effectiveness of BIA reorganization procedures in an ideal-conditions scenario. Following this logic, it would have been possible to suggest that any weaknesses or limits observed were at the lower limits compared with the entire population. But it turned out, based on the progress grids and the average indicators of degree of advancement developed in Appendix A, that all public companies were very representative of the total population.

In order to conduct a detailed analysis of the use of BIA reorganization procedures, the thirteen companies that had completed the procedure were selected from among the twenty-two public companies. Appendix B of the report discusses the thirteen detailed case studies. Part 2 of the report summarizes the results.

The choice of methodology for the case studies was motivated by the goal of analyzing the procedures in the context of companies' evolution. The other motivation was the desire to understand in a little more detail the workings of the current national system of business reorganization. While important, legal reorganization procedures are only one element of the national system that involves the evolution of a variety of institutions, some of which are private (credit rating agencies and commercial lending institutions) and some statutory or governmental (government commercial lending and investment agencies). Case studies can help us to better understand the different aspects of the regime.

The national system proposes an alternative to the BIA reorganization procedures for larger insolvent companies (those having debts of more than five million dollars). This is the CCAA, which is both less rigid than the BIA procedure, particularly in terms of timelines, and more

closely supervised by the court. The total number of case studies was brought to twenty with the inclusion of seven CCAA case studies.

Because until very recently, the number of companies having had recourse to a CCAA procedure before the courts of the Province of Quebec was much more limited than the number of companies having had recourse to BIA procedures, there was no real issue as to selection. The number of CCAA case studies corresponds to the number of relatively recent cases completed by the end of 2003. Appendix C of the report discusses the seven detailed CCAA case studies. These are all very exploratory. A short synthesis of the results, including comparisons with BIA reorganizations, is presented at the end of Part 2 of this report.

The conclusion contains five sections. It offers first of all a brief reminder of the scope of the study, followed by a discussion of certain results and the questions that they raise. The third section deals with the optimal choice between the different types of procedures, followed by considerations of effectiveness. The last section provides recommendations with regard to the operational and informational aspects of the procedures.

PART 1

EFFECTIVENESS, ACCESS TO REORGANIZATION PROCEDURES AND GOVERNANCE

Defining effectiveness

On the economic front, effectiveness will be well served by a law that allows people to interact at the lowest cost, i.e., that provides for reducing transaction costs. There are various ways to institute legal reorganization procedures, and we cannot simply presume that a specific law, for example, the BIA or CCAA reorganization procedures, contributes as much as it can to the efficiency of the economic system. Where that is not the case, we may speak in terms of an ineffective law. More concretely, a law will be effective if, first of all, it adequately covers its area of application, and secondly, if it does so at the lowest cost. We can say that a law covers its area of application if it governs the situations for which it was designed and does not apply in other situations.

The area of application of a law can be defined in terms of conditions of access to the procedures of said law. Figure 1 represents the possible inefficiencies of a company reorganization law in terms of access to its procedures under varying circumstances. The law will be effective if all companies for which reorganization procedures would be beneficial have access to it, at the right time, i.e., neither too early nor too late, and if the sought-after results are attained at the lowest cost.

Not all of the information is available at the start to allow for a determination of whether the application of a reorganization procedure to a company in financial difficulty will provide for a turnaround. For example, the creditors' reserve price is not known, i.e., the maximum rate of debt write-off above which they will refuse to support the proposed arrangement. And in terms of enforceable contracts, the reserve price of the suppliers of goods and services is unknown. For example, we do not know the minimum salary rate below which employees providing human capital specific and essential to the company will refuse to compromise.

In any context of trade or transaction at negotiated prices, the capacity of the parties involved to realize a beneficial transaction is conditional on the nondisclosure of their respective reserve prices. A reorganization procedure has a chance of being successful if the parties involved are convinced that the procedure will provide for fair partial disclosure of the reserve price of each party involved. Effectiveness therefore does not imply that the uncertainty involving the prospects of success of a reorganization procedure be eliminated from the start, but rather that procedures be initiated for all companies for which it is reasonable to make an attempt at reorganization, based on the information available at the time.

Figure 1 identifies three types of business. Group I represents businesses that could potentially benefit from reorganization procedures. Effectiveness implies that these businesses avail themselves of the procedures, and that they do so at the right time. The selection conditions provided for in the law should therefore not restrict access to the procedures, nor encourage using them at the wrong time, for example, when it is too late to effect a turnaround. The businesses in Groups II and III are those for which reorganization procedures should not be available. One characteristic of reorganization procedures is that they support keeping the existing management team in place. An effective law should therefore include provisions to ensure that easily accessed information is used quickly so that an insolvent company in the hands of incompetent management does not have access to a reorganization procedure, or that it makes use of the procedure for as short a time as possible. It goes without saying that rarely is incompetence immediately obvious; and what's more, a finding of incompetence should be preceded by a normal learning process.

An effective law should also include provisions to ensure that easily accessed information is used quickly so that a company in the hands of opportunistic management makes use of a reorganization procedure for as short a time as possible. The opportunistic managers of a very insolvent company might wish to use the reorganization procedures in order to put off

the company's liquidation as long as possible, allowing them to consume a greater portion of its residual value. Opportunistic managers of a company that is not or is only slightly insolvent might wish to use the reorganization procedures to "tax" to their advantage the shares of other parties involved with the company, like creditors or minority shareholders. Another motivation for opportunistic managers to avail themselves of the procedure is that it could enable them to challenge contractual rights or free themselves from legal obligations, involving the environment, for example.

The management team is generally the primary source for available information. Considerations with regard to the information available therefore implicitly involve parties other than the managers, particularly trustees and controllers, whose actions could determine access to the procedure and progress within it. Trustees and controllers, given among other things the cost constraints of gathering all the information that might be relevant, are very dependent on management teams, at least in the beginning. An effective law should not only include provisions for ensuring that the available information is used, but also incentives for management teams to share the information and exercise some self-discipline with regard to using reorganization procedures.

The companies represented in Figure 1 do not represent all the companies likely to be affected by a law on commercial insolvency. In addition to reorganization procedures, this law provides for liquidation procedures in the case of companies for which it is neither reasonable nor desirable to hope for a recovery. Effectiveness of the law implies that the selection conditions, or terms of access to liquidation and reorganization procedures, allocate insolvent companies to one or the other of the two types of procedures by taking into account the information available.

Figure 1 has a vertical bar representing access to reorganization procedures. This representation is relatively simplistic because it does not recognize the possibility of gradual entry into reorganization procedures through increasingly restrictive conditions leading up to the point where a proposal is approved, giving "new life" to the insolvent company. The philosophy underlying the BIA reorganization is based on gradual access to the procedures. The progress grids in the figures presented in Appendix A identify the terms of this gradual access. Such access can offer increased latitude for including provisions and incentives as discussed above.

Figure 2 provides for a different characterization of the companies in Figure 1; this time in terms of changes in performance rates. First, as represented by the solid line, there is a constant reduction in the profit rates of the company that will eventually lead to negative profits and a state of insolvency. Reorganization procedures then enable the company to improve its performance, although it still remains negative.

In the second case, represented by the dotted line, the company was profitable up until an event, referred to as a hiccup, served to drastically compromise its profitability and pushed it rather quickly into a state of insolvency, after a short period of very negative performance and increasing debt. Reorganization procedures then enable the company to bring its indebtedness to levels it can support and if necessary, enable it to revise certain clauses of non-financial contracts. There follows an appreciable improvement in performance and the company returns to profitability.

Informational constraints and governance

Referring to Figure 2, an effective law should reserve reorganization procedures for companies whose performance corresponds to the dotted line, and disallow the procedure in cases represented by the solid line. Referring to Figure 1, an effective law should in all probability reserve reorganization procedures for companies in Group 1. The challenge on the informational and behavioural fronts is to implement a system that provides those concerned with the means and the incentives to quickly make the distinction between the two

types of cases. As mentioned in the Introduction, this challenge raises governance issues. How do we ensure that the agent, who is the main source of information, acts in the interests of the principal? In the context of a reorganization procedure, the actions of the agent refer in particular to the sharing of reliable information with the other parties involved in the procedure. The next Figures 3 to 6 use the distinction between “principal” and “agent”, dear to the theory of governance, to identify the status or role of the various parties involved with a company, depending on whether it is solvent or insolvent, its size, and whether it is using a reorganization procedure.

Figures 3 and 4 apply to SMEs likely to avail themselves of BIA reorganization procedures. The construction of these figures assumes that the same person combines the functions of management and ownership of the company. If the company is solvent, the entrepreneur and manager, the same person, is both agent and principal (Figure 3). If the company is insolvent but there is no reorganization procedure, the trustee becomes the agent. If there is a reorganization procedure, the entrepreneur-manager remains involved with the trustee as agent of the creditors and the other parties involved, such as representatives of workers or the local community.

For larger companies, we should distinguish between the shareholders and the management team. If the company is solvent, the former assumes the role of principal and the latter, of agent. If the company is insolvent and there are no reorganization procedures, the body of creditors becomes the principal and the trustee is their agent (Figure 5). If there is a reorganization procedure, such as the one provided for in the CCAA, the trustee, called the monitor, shares with the management team the role of agent of the creditors and other parties involved in the company (Figure 6).

As previously discussed, reorganization procedures raise governance problems. Given that in a situation of insolvency the governance context is very different for SMEs than for large companies, as illustrated by Figures 3 to 6, it is reasonable to assume that the effectiveness of the law requires reorganization procedures that are not at all identical for these two categories of company.

PART 2

ANALYSIS OF THE CASE STUDIES

In order to have a reference framework for evaluating the representativeness of companies selected for the case studies, the use of BIA procedures in the Province of Quebec over the period 1998-2003 was analyzed on a global level. This global analysis included a base population of 3,000 incorporated businesses. The results of this analysis are reproduced in Appendix A. The entire procedure is represented by a diagram (Figure A.8) that breaks the process down into two sub-processes, one before and one after court approval of the proposal. This stage constitutes a turning point in the procedure. Before court approval, the BIA procedure imposes requirements and timelines that must be respected by the debtor company or it will be deemed to have assigned its assets and be liquidated. After court approval, the company regains its autonomy, subject to performing the conditions defined in the proposal. The effective constraint represented by these conditions can vary a great deal from one proposal to another.

After the exploratory study of the percentage distributions of companies in the base population (Tables A.2 to A.7) was completed, a code was attributed to each stage of the procedure in order to describe the progress of this population through it. An indicator of average stage reached in the procedure was defined and estimated for the base population and for the sub-groups, depending on activity sector and region (Tables A.8 to A.21). The indicator values demonstrate that on average, in terms of the total population, reorganization procedures terminate between the stage at which the proposal is approved by the meeting of creditors and the stage at which the proposal is approved by the court. This overall result varies appreciably among the sub-groups based on sector, region, and other variables such as the value of assets reported when procedures were initiated.

Companies that have sought BIA protection

Process for selecting the cases for analysis

As previously explained, after the exploratory case studies with companies in the manufacturing sector, the choice of companies to be used for case studies for analyzing BIA reorganization processes was limited to public companies. In order to be able to analyze the quality of the financial and accounting information communicated by companies that had availed themselves of the BIA, we first had to ensure that such information was available. It was therefore agreed that we would concentrate on public companies, as they are obliged to communicate information to the public, particularly their financial reports. This choice could have led to bias. Because market regulations obligate these companies to disclose information, it is reasonable to expect that reorganization procedures be initiated and take place in an atmosphere of greater availability of information. If so, it would have been reasonable to assume that the use of these procedures would be more forward-looking than the use made by private companies in the base population. On the basis of progress grids and the values of the indicator of average stage reached, it appears that status as public company is not a source of differentiation.

In order to identify public companies, the list of companies included in the file provided by the Office of the Superintendent of Bankruptcy (OSB) was compared with the list of companies on the Sedar Web site. Twenty-two companies that are found on both lists comprise the population of public companies that undertook legal reorganization procedures from 1998 to 2003. Thirteen companies were selected from this population. Of these thirteen companies, four did not succeed in having their proposals accepted, while nine completed this stage. Of the latter, five companies terminated their procedures, only three of them successfully; success being defined by the closing of a file without notice of default in the performance of the terms of the proposal. It should be mentioned that a file is closed when the trustee presents his or her final statement of receipts and disbursements and is discharged by the court.

For the thirteen companies studied, the information collected includes the documents presented by the debtor as per the BIA, the financial reports available on the Sedar site, and articles that appeared in the Quebec media. In a few cases, meetings took place with the trustee involved.

Appendix B describes the thirteen case studies, beginning with those that completed the procedures and ending with the least advanced case. Figures 7 and 8 represent the level of advancement of the thirteen companies in the BIA reorganization procedure.

Summary of BIA cases

Table 1 presents some general characteristics, grouping companies based on progress, and where applicable, the result of the procedures. The first column on the left identifies the company and indicates the date on which it filed its notice of intention to propose a reorganization plan to its creditors. The next column describes the nature of the business. The samples include a construction company (LBL Skysystems), two companies from the mining sector (Ressources MSV and Exploration Lesseps), four companies from the manufacturing sector (Sofame, Protec, Naya and Ultravision) and six service companies. This distribution of cases by primary, secondary and service sector approaches the breakdown of economic activity on the global level.

We should point out as well that 12 of the 13 companies studied filed applications for time extensions, with Environair Sipa being the exception. One of the companies, LBL Skysystems, even found an original way to exceed the time provided for in the Act. A priori, it would appear that there is a link between length of procedures and results, the less problematic files proceeding more quickly. This link, which was partially supported by the results on the global level (see Appendix A), was not confirmed by the case studies.³

Given the stated objectives of the Act in terms of maintaining economic activity and jobs, one might think that there would be pressure on the creditors to approve reorganization plans for companies with numerous employees. The case studies negate this theory: those companies having the most employees were not able to have their plans approved, or didn't file them.

The circumstances and the grounds for resorting to legal reorganization procedures do not emerge clearly from the documents examined. The causes of the difficulties presented in Table 2 are not very detailed, and they correspond to those identified by the debtor. The hiccup theory is used to justify recourse to the procedures in only the following files:

- Bridgepoint suffered as a result of the September 11, 2001 terrorist attacks;
- The death of the President of CQI Biomed disrupted the company;
- LBL Skysystems had problems with its control system.

In addition, corrective measures chosen by the debtors to resolve their financial difficulties were not linked to the diagnosis of the causes of the difficulties presented in the file. This observation may be surprising, at least for companies that want to remain in operation. The first step in resolving the problem involves identifying the problem, defined here as being the debtor company's financial difficulties, to identify its causes, and to then attempt to remedy it through actions that are related to these causes. Some examples include diversification or rationalization of activities through de-integration before or after the event, or the withdrawal of certain products or services. The files analyzed didn't allow for making the link between the causes of the difficulties and the recovery methods planned by the company. Creditors have little or no information, at least on paper, to enable them to determine whether the measures proposed by the debtor are likely to resolve the difficulties.

3. It would also be interesting to examine the impact of the amount of time taken on the costs of the procedure. Martel (1994) concluded that each additional day of the procedure cost \$24.

Table 3 shows that of the eleven companies that filed a reorganization plan, only four (Sofame, Cenosis, Exploration Lesseps and TMI-Education.com) appeared to want to continue operations and maintain ownership of assets. Some of these proposed that their creditors exchange their claims for shares issued by the company. The reorganization plans filed by the seven other companies were aimed more at liquidating or transferring assets to parties outside of the company.

In the cases of “reorganization” for purposes of liquidation, the analysis of the files does not indicate whether the potential buyers that were approached or chosen had links with the company’s management or current shareholders. This could be a deficiency in the existing procedure. From the point of view of the objectives being pursued, would it be preferable that the creditors, whom the debtor company is asking to write off a large part of their claims, know to whom and under what conditions the company’s assets will be transferred⁴?

Table 3 also reveals that the majority of companies whose plans are accepted by the creditors anticipate the presence of inspectors during the performance of the plan. This mechanism provided by the BIA seems to be appreciated. From the company’s point of view, it allows for some flexibility in implementing the plan, while from the point of view of the creditors, it constitutes a means of both control and access to information.

The same table also shows the time anticipated by the company to reimburse the unsecured creditors. According to Fisher and Martel (1996)⁵, a short time period is a signal that the company has the necessary resources to successfully carry out its plan. Once again, the case studies did not provide for validating this theory on time periods. It is reasonable to assume that the creditors base their decision on both the time it will take to be paid as well as the amount of the dividend. They are no doubt seeking the optimal balance between a short time frame and its probable negative impact on the amount of dividends.

Of the six companies eligible for the CCAA, identified in the right hand column of Table 3, half did not file a proposal or were not successful in having it accepted. Once again, the limited number of files dictates caution in drawing conclusions; this result suggests that companies whose level of debt makes them eligible for the CCAA nevertheless resort to a BIA procedure. This recourse to a BIA procedure could be explained by the desire to have some time before assets are liquidated, or by difficulties whose sudden magnitude requires a speedy response, which comes in the form of the notice of intention in the BIA procedure.

The results of creditors’ votes on reorganization plans are presented in Table 4. The reported cases suggest that beyond the regulatory requirement for creditor approval for undertaking a procedure, half-hearted approval from the ordinary creditors participating in the procedure, i.e., who have filed a proof of claim, is a good indicator of the proposal’s chances of success. Among the creditors participating in the vote on the proposal, directly or through representation, there would appear to be at least a few who are in a position to distinguish between plans that are likely to succeed and those likely to fail. Similarly, a lack of consensus among the creditors would decrease the chances of success of reorganization plans.

It is also interesting to note that when the trustee documents his or her position with regard to a reorganization plan, as indicated in the right-hand column of Table 4, this position is favourable in seven out of eight cases. Some trustees feel that the very essence of their

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4. Does this raise, for example, an issue of fairness as discussed by the Senate Standing Committee on Banking and Trade in its report dated November 2003, in which it held that jurisdiction in insolvency matters should target fairness? If the creditors experience losses, it would seem appropriate that they know about the losses being absorbed by the other parties involved with the company. On this front, it was reported to us that companies that seek protection under the American law must make public any purchase offers that they receive. Would it be worthwhile to amend Canadian laws in the same way?
 5. Fisher T.C.G. and J. Martel. *Should We Abolish Chapter 11? Evidence from Canada*, Scientific Series, 96s-22, CIRANO (1996), 1-41.

mandate is to help the debtor to file a plan that will be acceptable to the creditors. Others believe rather that they should maintain their independence from the debtor and that consistent failure to recommend rejection of the plan could harm their credibility.

Table 5 reveals that the percentage of write offs of ordinary claims generally exceeds 90%. It is difficult to identify trends with the other statistics presented in Table 5. For example, the percentage of total receipts out of the total amount of proven claims varies a great deal. It is less than 1% in the case of Protec, and 48% in the case of Ressources MSV. Based on a preliminary assessment, the amount of total receipts does not appear to be related to the length of the procedures (centre column of Table 1), because Protec's procedure lasted for 24 months, while that of Ressources MSV only took 14 months.

Finally, the centre column in Table 6 clearly shows that companies or their trustees disclose very little information that would allow creditors to compare scenarios for accepting or rejecting the plan. With the exception of the Sofame case, the files contain only a few offhand remarks confirming that, in the event of bankruptcy, ordinary creditors would receive a "smaller" dividend, without quantifying it, or "no dividend".⁶

The last column on the right of Table 6 provides a few examples of the questions that remain unanswered after reading the documents filed with the court. In reality, one of the main conclusions that emerges from this research is that the documents recorded in the files contain relatively little factual information to allow creditors to make an enlightened decision on reorganization plans.

6. While some files contain a comparison of liquidation value vs. book value for certain assets, these comparisons remain too partial to provide for a reliable projection of liquidation dividends based on each scenario.

Companies that have sought CCAA protection

Process for selecting the cases for analysis

As explained in the introduction, there was never really any question as to how to select CCAA cases given the period covered, the advantages of dealing with closed files and the fact that for purposes of comparison with BIA cases, the research focused on cases presented before the courts in the Province of Quebec.

Summary of CCAA cases

The CCAA case studies differ from the BIA case studies in the following ways:

- The seven CCAA case studies cover the mining, manufacturing and distribution sectors.
- One company among the seven, Mines McWatters, filed its proposal after more than six months, i.e., beyond the maximum period that could have been approved had it chosen a BIA procedure for its reorganization.
- The companies analyzed employed an average of 196 people, with the numbers ranging from a minimum of 48 to a maximum of 600. On this front, they are therefore larger than the majority of companies that avail themselves of the BIA (Table 1).
- Three companies among the seven CCAA cases were subsidiaries or divisions of multinational companies: Eicon, PCI Chimie Canada and Produits Nautiques Altra. In the latter two cases, the American sister organization also applied for court protection in order to try to recover.
- One company among the seven cases explicitly attributed a hiccup to the cause of its difficulties. That was Mines McWatters, which mentioned unanticipated obstacles and delays in relocating a road.
- Of the seven companies, there were two – Produits Nautiques Altra and Services de roulement Harvey – whose arrangement plans turned out to be asset liquidation plans. The five other companies filed plans aimed at keeping their operations going.
- With CCAA cases, it is more difficult to estimate the level of credit write-offs, particularly because of the sometimes significant conversions of debt to share capital. For plans whose terms did provide for a quick estimate of a debt write-off rate, this rate varied between 14 and 90%.
- Only one file contains an estimate of dividends in the event that the plan is rejected.

Information and control

Financial and accounting information

The files analyzed differ in terms of the accounting and financial information communicated to creditors. For example, some files do not explicitly mention the value of asset liquidation, the majority don't describe the underlying assumptions in the determination of this value, and finally, none deal with the uncertainty surrounding these estimates. While the trustee's role may not be to verify all of the information, particularly in view of the urgency of the file or the fees that he or she can reasonably charge the debtor, the fact remains that a lack of information is problematical. If it were proven that creditors lose more money where there is bankruptcy rather than reorganization, it might not be appropriate to burden the process with new information requirements. But it would be difficult to prove this claim, often put forward by trustees. Observing that average dividends to creditors in reorganization procedures are higher than dividends to creditors in liquidation procedures does not imply, a priori, that one procedure is preferable to the other in terms of dividends. It would be difficult to prove a

theory that maintains that the type of insolvency procedure is an important determinant of the dividend rate paid to creditors.

The dividend rate is fundamentally a consequence of the general health of the company at the time that it undertakes the procedure. In order to be able to attribute a causal relationship to a correlation observed between the type of procedure and the dividend rate, we must make the assumption that the type of procedure conditions this general health. This could be the case if, for example, reorganization procedures were more conducive to a premature reaction from the company to its state of insolvency, with the result that it undertakes a BIA procedure earlier, and therefore with more assets.

In the majority of BIA files, reorganization procedures were used for purposes of liquidation. A hypothesis that takes into account a higher average dividend rate in reorganizations than in liquidations would be that, in the current legal context, it is preferable to proceed to liquidating companies that still have significant assets by using reorganization procedures rather than liquidation procedures.

Some files raised the crucial question of whether all the assets held by the debtor were still under its control. The most problematic cases are those in which some affiliated companies place themselves under the protection of the law while others don't. This question is of particular importance from the point of view of the principle of fairness for all the parties involved with the same company. One way to answer this question would be to compare the list of assets included in the last statement of affairs preceding the date of the notice of intention with the list of assets on hand on the date that the trustee accepted his or her mandate. While some files include a comparison of certain book values with certain liquidation values, the list of assets is rarely available.

Projected cash-flows should be an important consideration in the decision of whether to undertake a reorganization procedure. The BIA reorganization procedure requires that this information be added to the file within ten days of the filing of the notice of intention. The CCAA requires that "any material adverse change in the company's projected cash-flow" be reported to the court by the monitor forthwith after it is ascertained. Some companies file projected deficit cash-flow statements. Strictly speaking, this means that continuing operations will not provide for maintaining the basket of assets, which would run counter to the interests of the body of creditors. Under such circumstances, it would be most appropriate to provide justification for pursuing the reorganization procedure. For example, is it reasonable to hope for a higher sale price for the company's assets in the long term? The files also show that cash-flow statements cover different periods, running from a few weeks to several months, and have different levels of detail. For example, some statements contain several columns showing weekly projections, while others contain only a single column of figures setting out the total. Finally, in reviewing the information provided for the assumptions used, we note that companies only show the results of asset liquidation as of the date of the notice of intention, even if they wish to continue operations.

Control by creditors and participation

An examination of several files as well as interviews with some trustees reveal that few creditors attend the meetings, and that only a proportion of them file a proof of claim giving them the right to be a party to the procedure. Data related to this aspect of the procedure were compiled in a first sample composed of manufacturing companies with assets of at least \$1M.

The number of creditors having proved their claim and therefore permitted to vote on the proposal, directly or through proxy, represented 37.7% of the number of ordinary creditors identified on the list prepared by the debtor at the beginning of the procedures. We can only speculate at this point as to the reasons for this: are the creditors convinced that they have already, for all intents and purposes, lost the money loaned to the companies? Do they feel they lack the information to make an informed decision? Do they feel that the amount of their claims does not justify spending the time and the money for representation? Do they

think that other creditors who are better informed and more affected will be present to defend the interests of all creditors?

It may be that creditors serve as an effective means of control only if the risk of greater losses associated with non-participation in the procedures is sufficiently high to justify their involvement and if they believe that they have enough information to make an enlightened decision. In the current context of generally low dividends in almost all cases, the risk of greater losses in case of non-participation is really quite limited.

CONCLUSION

As with organizations in general, companies exist because ongoing contractual relationships can generate value. This type of contractual relationship is studied in the theory of governance. Because it threatens the survival of a company, insolvency can put an end to contractual relationships that are designed to continue over time. Legal reorganization procedures are aimed at establishing a governance regime for insolvent companies that will preserve as much as possible the contractual relationships that have been developed within the company. An analysis of the effectiveness of these procedures involves evaluating their success in attaining this objective.

Governance deals with the whole set of social interactions among the parties involved with a company. These interactions are not easily observed, particularly in the context of a painful revision of contractual clauses, as is the case with insolvency. At the empirical level, the analysis of effectiveness is therefore based on artifacts flowing from the procedures, combined with the social interactions that they govern, and not on the interactions as such. Given these limitations, we must be modest when drawing conclusions and making recommendations based on the research. The case studies constituted exploratory research, a clearing of the undergrowth so to speak, and really, a learning experience.

Scope of the research

This research project was intended to analyze the effectiveness of reorganization procedures under Canadian commercial insolvency legislation. The methodology used to conduct the research involved a series of case studies of companies that had availed themselves of reorganization procedures. Twenty case studies were conducted, broken down into two sub-groups: a first group of thirteen companies that had used BIA procedures, and a second group of seven companies that had used CCAA procedures.

Reorganization procedures are aimed at specifically reorienting the fate of the company using them. The choice of a case-study methodology is motivated by the desire to analyze the procedures in the context of the company's evolution. For each company in the study, the research consisted of three components: a first component dealing with the conditions of recourse to the procedure, a second component on the history and circumstances of the company before recourse to the procedures, and a third component on the results of the use of the procedures, including following up on the company after it emerged from the procedures.

Legal reorganization procedures are intended to enable companies that have potential, but are temporarily insolvent, to turn themselves around. The appropriateness of such an objective is hardly debatable. However, in interpreting the results obtained in pursuing this objective, the analyst is confronted with a certain complexity or ambivalence. For example, how do we concretely define the notion of recovery or reorganization of an insolvent company?

Results and questions

In terms of the BIA procedure, the first general impression that emerges from the case studies is of the effectiveness of the control mechanism aimed at preventing inappropriate use of the procedures by companies that do not have potential for recovery. A simple notice of intention filed by the trustee who has consented to act as trustee in the file of the company in difficulty provides for a stay of all creditors' remedies. In order to control abuse, the legislator attached to the procedure quite strict time periods, some of which can be renewed a limited number of times by the court pursuant to an application justifying the extension. At each prescribed stage, one or more of the case studies were eliminated from the reorganization procedure and automatically transferred to BIA liquidation procedures. On this front, the population of public companies used for the case studies, which represent barely 1% of incorporated companies that availed themselves of BIA reorganization

procedures, is representative of the whole. It is important to emphasize that effectiveness of the control mechanism does not imply that it be sufficient to prevent all inappropriate forms of use of BIA reorganization procedures.

The public companies are also representative on the global level. By coding each stage of the BIA procedure, it was possible to calculate the average stage reached within the procedure for public companies having recourse to the BIA, and for the total population of incorporated businesses having recourse to BIA reorganization procedures. For both groups, we can see that the reorganization procedure terminates between the stage where the creditors approve the reorganization plan and the stage where the plan is approved by the court. In other words, on average, it is more likely that a notice of intention will give rise to a procedure that is terminated before the proposal is executed, than to a procedure that makes it to that stage.

In view of the greater availability of information, or the greater transparency of public companies, we anticipated from the start a more selective application of BIA reorganization procedures, and as a result, a greater probability that the procedure would lead to a reorganization plan that is accepted and completed for public companies. This expectation was not realized.

As with all governance regimes, the dissemination of information plays a critical role in reorganization procedures. The various stages of the BIA procedure mark points of information dissemination. The thirteen BIA case studies reveal a certain lack of consistency in terms of the numbers available to creditors. The trustee remains very dependent on the debtor company for any information that he or she does disseminate. While the trustee is not intended to play the role of auditor, it is understandable that this situation can be a problem from the creditors' point of view.

The trustee's report presents a statement, generally brief, with regard to the causes of the debtor company's difficulties. Often, the statement repeats almost word for word the causes identified by company management. Moreover, the terms of the proposal presented to the creditors, in the case of procedures aimed at continuing operations rather than liquidation, are not linked to the causes of the difficulties.

In order to enlighten the creditors with regard to the choice between supporting the proposal being made to them or rejecting it, the trustee's report presents estimates of the value of the company's assets in the event that the proposal is accepted and estimates in the event that it is rejected. The underlying assumptions for the first estimate are rarely described; the estimate of the value in case of bankruptcy or liquidation is even less often documented. There is no discussion of the uncertainty of the estimates, either. This situation is conducive to bias in the accounting information. Moreover, given that in the majority of companies studied, reorganization procedures are used for purposes of liquidation, the estimate of the value of the assets in the event that the proposal is accepted most often measures a liquidation value. This therefore raises the question of the interpretation of the estimate of the value of the assets in the event that the proposal is rejected. We are faced with two liquidation values without knowing exactly what differentiates them. The first liquidation value would correspond to a current purchase or finance offer, while the second liquidation value would correspond to the value of liquidation expected in the event that the current offer is rejected. Under these circumstances, would it not be appropriate to proceed to a sale by pre-advertised public auction conditional on the creditors' acceptance of the best offer?

Proposals almost always benefit from external financing, which is especially true for BIA cases. In cases of liquidation proposals, this financing corresponds to the amount paid by the future owner of the company to the various classes of creditors to acquire the company's assets. With a proposal aimed at continuing the company's operations, the external financing generally corresponds to the dividends paid to the ordinary creditors in order to obtain their agreement. If there is negative cash-flow for the reorganization period, or part of that period, the external financing also includes the funds required to cover the deficit. The information disseminated with regard to the proposal does not systematically identify the source of the

external financing, nor does it provide details about the relationship between the external source of financing and the owners or managers of the debtor company.

In some cases, there were among the institutional lenders governmental or quasi-governmental agencies mandated to ensure adequate funding to businesses likely to suffer from credit rationing. Some of the results reported in Appendix A suggest that the reorganization procedures could constitute a corrective or compensatory mechanism to the credit rationing faced by certain business categories. If that is the case, it might make sense to verify whether or not the existence of governmental or quasi-governmental financing observed in the files studied is simply a coincidence.

With both BIA and CCAA procedures, creditors represent an effective means of controlling the use of reorganization procedures by a debtor company if, first of all, they participate in the procedure by proving their claims and attending or being represented at the meeting of creditors. Secondly, the creditors must have sufficient reliable information. With regard to the decision to participate, and as previously discussed, it would appear that creditors make a judgment call between what they stand to lose if they don't participate, and what they stand to lose if they do. The generally low levels of dividends in both cases and the temptation to be a freeloader can explain the low rate of participation observed in BIA cases. This observation was confirmed in conversations with trustees. The participation of creditors being an important component, if not the main component, of the control mechanism designed by the Act, their very low participation raises the question of effective control of the procedure. This issue is particularly important on two levels: when negotiations are ongoing to develop a proposal that appears acceptable; and when the proposal is presented for approval. Given this low rate of participation and given that the BIA procedure seems to be used principally for liquidations, it might make sense to introduce into the current reorganization procedures provisions for some OSB control over liquidation procedures.

The CCAA procedure is intended to be more flexible than the BIA reorganization procedure. This flexibility has a cost in terms of the legal and paralegal fees associated with the court's supervisory role. The flexibility should a priori provide for recognizing the specificity of each case and for making more optimal reorganization decisions about it. The seven CCAA case studies show considerable diversity in circumstances that would have been difficult to accommodate under a BIA reorganization procedure. More fundamentally, and for the majority of cases, over the course of the procedures, the court had to rule on very specific questions dealing with contractual clauses interfering with the reorganization procedures or compromising their chances of success. From this standpoint, the CCAA procedure would appear to have been more appropriate. But we reach that conclusion with some reservation given that the CCAA case studies were of a more exploratory nature.

Optimal choice between BIA or CCAA liquidation and reorganizations

Based on the sampling of case studies, it would appear that effectiveness of use in terms of the choice between a CCAA procedure and a BIA procedure is relatively good. We did find a few companies that opted for a BIA procedure when their size and the complexity of their situations warranted a CCAA procedure. In a few cases that were in all likelihood CCAA-type, the reorganization was initiated with BIA procedures, probably for reasons of urgency, given that the BIA offers a more speedy procedure than the CCAA for staying creditors' remedies. But just as quickly thereafter, the debtors involved used the legal provisions allowing them to transfer the file to a CCAA procedure.

Still on the effectiveness of use, but this time in terms of the choice between a reorganization procedure under the BIA and a liquidation procedure under the BIA, the research results raise more questions than the preceding situation. In the majority of BIA case studies, the result of the reorganization procedure was liquidation, and for some cases, liquidation was the stated intention right from the start.

Reflections on effectiveness

Defining the concept of the effectiveness of the legal reorganization procedures required reflecting on the nature of business in the Introduction to this report. The rules of cooperation between the parties involved in a company are defined in the contracts of specific application to that company and in the laws of general application in the area of business and labour relations. Different conceptual approaches provide for an analysis of laws in this perspective. The costs-of-transaction approach allows for a characterization of the effectiveness of both procedures and processes. The case studies illustrated how legal reorganization procedures can enable the parties involved, as well as new parties, to come to terms under conditions and circumstances that probably would have been too expensive to anticipate in the contracts concluded while the company was still solvent.

It would be simpler if we were able to maintain that effectiveness of the process leads to effectiveness of results. But until that can be demonstrated, it is useful to clarify the notion of effectiveness along the “results” dimension. Effectiveness is attained when all the costs and benefits inherent in a decision are taken into account. Legal reorganization procedures will be effective in terms of results if they enable insolvent companies to benefit from adjustments that satisfy this condition. The notion of the public interest generally refers to the costs and benefits that certain mechanisms of exchange and economic processes motivated by individual interests could tend to ignore. Along the same lines, and with the presumption that there can be a rather fine line between reorganization and liquidation, maximizing the net price of the insolvent company’s assets would constitute an operational objective guaranteeing the attainment of effective results.

Figure 9 depicts the effectiveness of commercial insolvency legislation in terms of maximum net price of the assets of insolvent companies, based on the type of procedure and length of the process. This representation is valid if we can maintain that the interests of all parties involved converge on this objective of maximum net price. Jobs are often evoked with regard to the public interest, and sometimes placed in opposition to maximum net price, the argument being that the creditors should agree to reduce their dividends in order to save more jobs. But is it not reasonable to suggest that a way to guarantee the maintenance or creation of the maximum number of jobs would be to allocate the assets of an insolvent business to those who value them most, and as a consequence to those who would make the best use of them?

The variance between the net price of assets and the price paid corresponds to the cost of the procedure. The professional services of trustees, lawyers, or accountants are a well-known example of this cost. In several files, the trustee was also appointed interim receiver for purposes of the sale of the assets. Given the powers accorded to the trustee in reorganization procedures, and given the role of the court in approving the sale of the assets, it might be desirable to reconsider the appropriateness of these distinct roles with the costs that they engender.

Recommendations

1. When the cash-flow statement presents deficit projections, it would seem appropriate to provide reasons to justify pursuing the company's activities within a reorganization procedure.
2. The analysis of the files does not indicate whether eventual buyers expected to finance the reorganization are related to the company's current management or shareholders. Given the interests of the other parties involved, it would seem appropriate that the report from the trustee or monitor to the creditors indicate whether such relationships exist. If they do, the report should provide a short description of the nature of these relationships.
3. In a reorganization procedure, the OSB has very little control over the process and the players compared with liquidation procedures. Given the low rate of creditor participation in BIA reorganization procedures, and given that these procedures seem to be used frequently for liquidation purposes, it would appear appropriate to ensure that existing control mechanisms are adequate.
4. It would be a good idea to explore the possibility of having files present a more detailed analysis of the causes of the difficulties and then creating a link between the measures anticipated in the proposal or arrangement and the causes of the difficulties that have been identified. One way of gathering and ordering the information might be to check whether, first of all, there were one or more hiccups at the origin of the company's difficulties or whether the state of insolvency is a result of problems of a more distant origin that will likely persist. Secondly, a classification of the anticipated measures that distinguishes between the creditors' financial concessions and concessions made in existing contracts, such as a lease or collective agreement, could be introduced. The discussion of the link between the diagnosis and the prescription could be guided by the preceding distinction and classification.

As previously indicated, the analysis of progress in BIA procedures revealed that public companies were very representative of the total population. It would be difficult to ignore, however, that these companies are more accustomed to communicating information. If informational deficiencies are observed in the case studies, it is reasonable to believe that they would be even more evident with private companies. This reinforces the recommendations, unless the existence of a public market for the shares of public companies creates incentives for management of accounting information in general as well as in the more specific context of reorganization procedures. In a different vein, if it is fair to consider legal reorganization procedures as being a means of ex post adjustment of multiple contractual relationships, then with the current economic context in which more and more adjustments are taking place and there are more and more calls for adjustment mechanisms, we should ensure that these procedures function effectively.

Figure 1
Inefficiencies in terms of access to procedures (dotted lines)

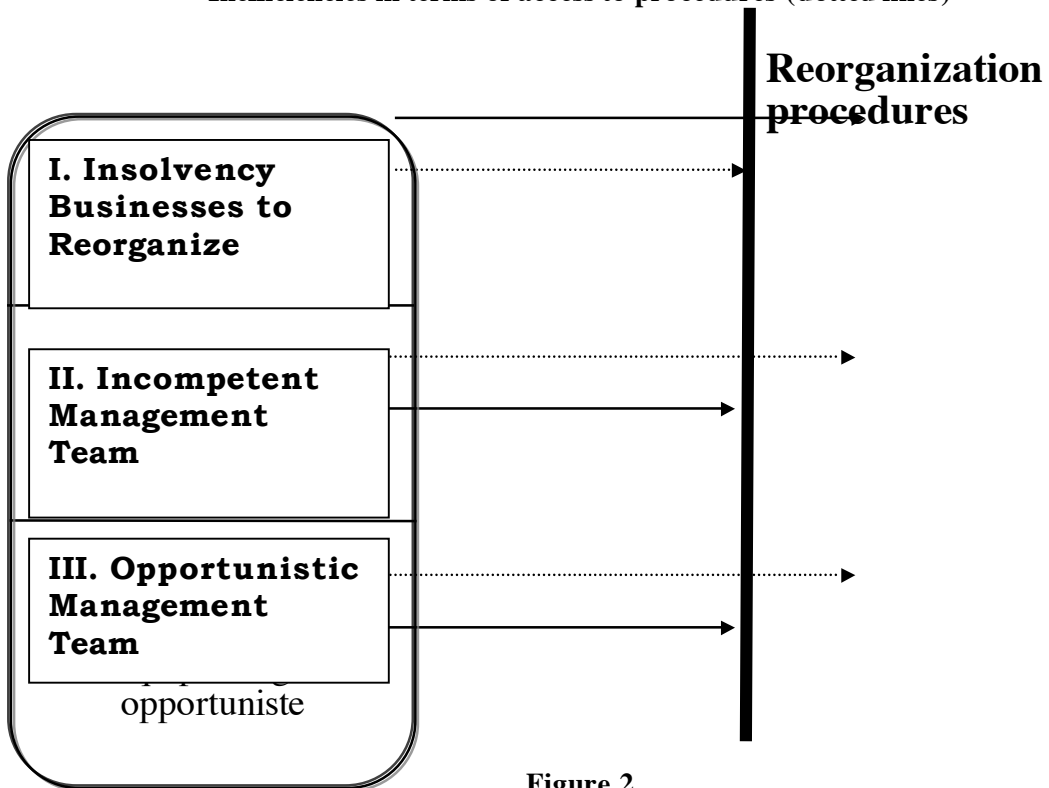


Figure 2
Elements of credibility: the hiccup theory

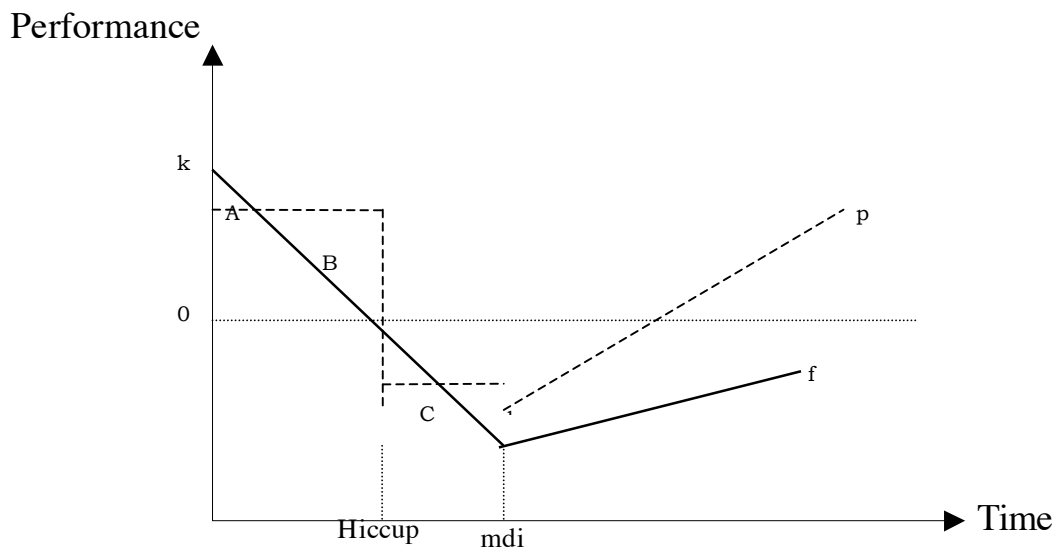


Figure 3
Insolvency: problem of SME governance
Without BIA procedure

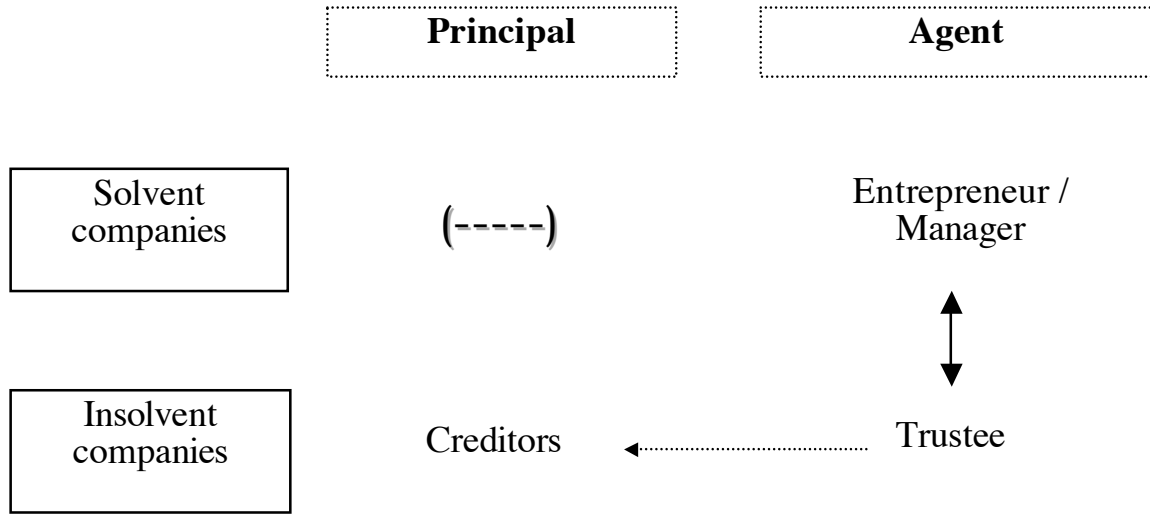


Figure 4
Insolvency: problem of SME governance
With BIA procedure

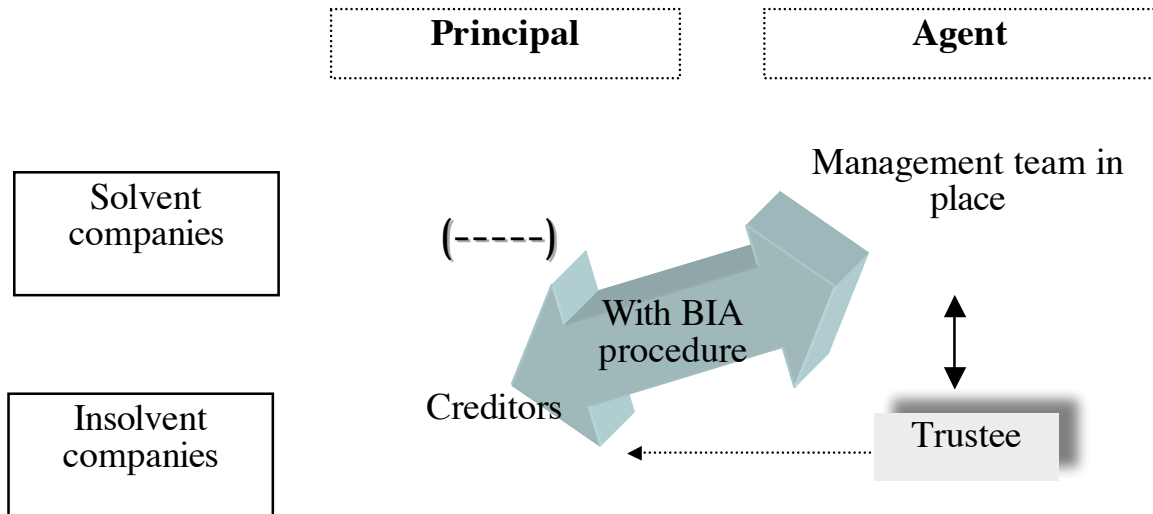


Figure 5
Insolvency: problem of governance – Large companies
Without CCAA procedure

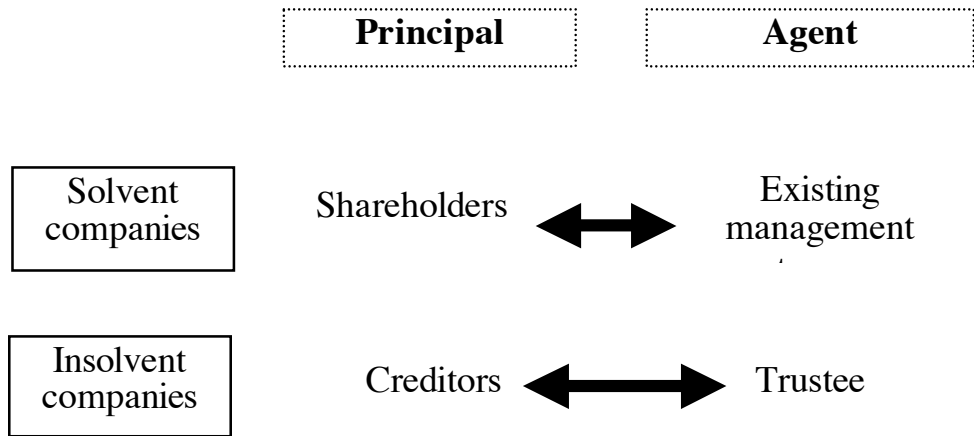


Figure 6
Insolvency: problem of governance – Large companies
With CCAA procedure

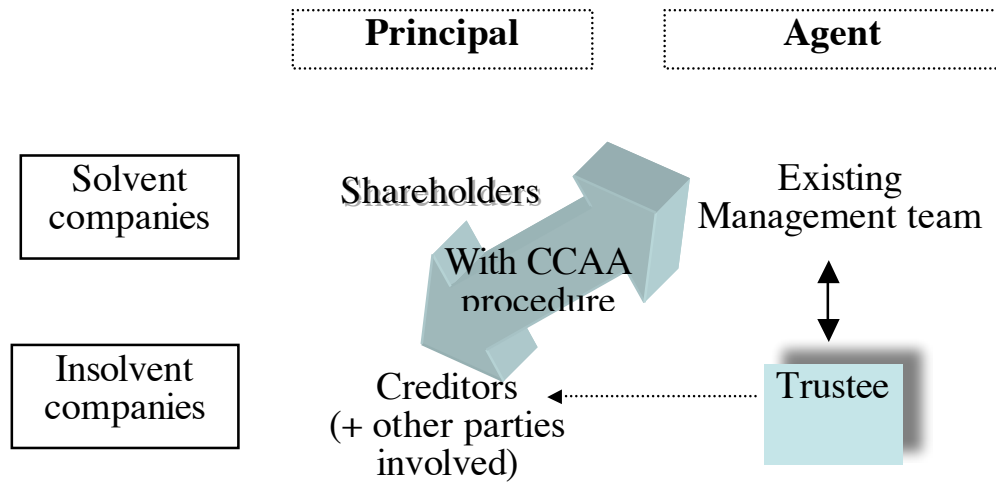


Figure 7
Progress of BIA cases under sub-process A

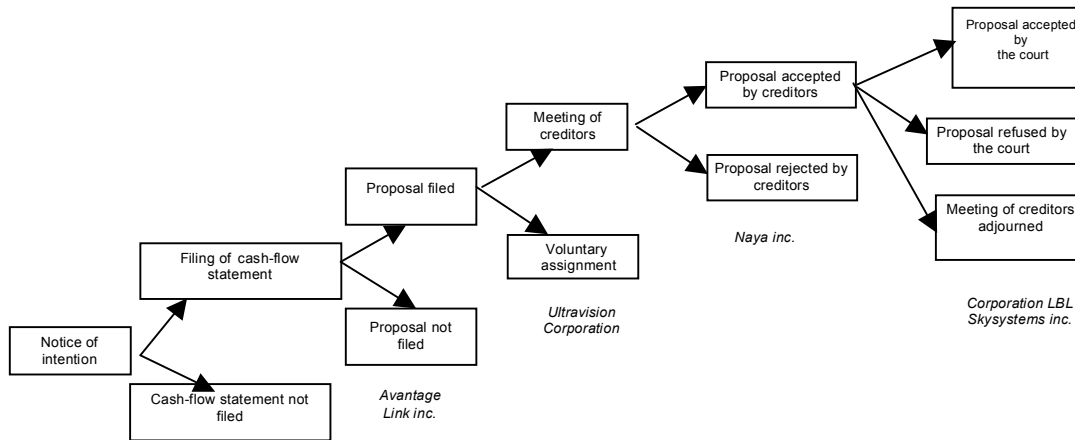


Figure 8
Progress of BIA cases under sub-process B

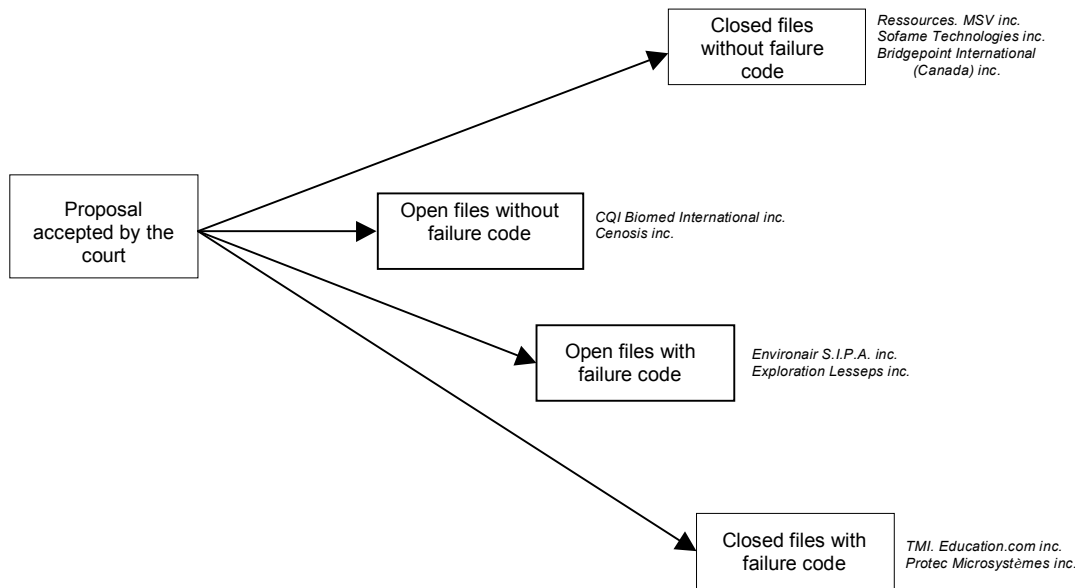


Figure 9

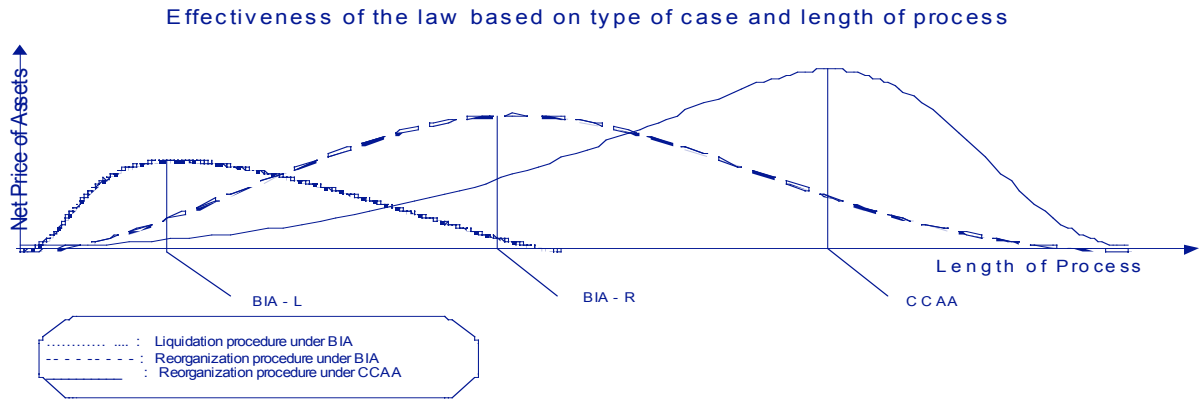


Table 1
General presentation of BIA cases

Activities	Duration of the procedure⁷	Number of jobs affected	Other comments
Companies that successfully completed BIA procedures			
Bridgepoint (November 2001)	Leasing of telecommunications space and equipment	18 months	About ten
Ressources MSV (September 2000)	Copper and gold mines	14 months	From 5 to 8 at the beginning of the procedure to 175 if the company survives
Sofame (January 2003)	Manufacture of heating appliances	20 months	18 Numerous management resignations. This is the only company that continued operations after the BIA procedures
Companies with ongoing files, without failure code			
Cenosis (February 2003)	Development and integration of publishing and communications software	Ongoing (for 31 months)	About ten <ul style="list-style-type: none"> • Strong external growth in 2000-2001 • Significant stock market price volume and volatility
CQI Biomed (December 1998)	Distribution of medical products that are either in the development stage or approaching the commercial production stage	Ongoing (for 81 months)	NA

7. From the notice of intention up to the final dividend (trustee's application for discharge), using the information available up to April 2005.

Companies with ongoing files, with failure code				
Environair Sipa (November 1999)	Industrial pollution management engineering	35 months (65 months including bankruptcy)	17 in November 1997 but none at the beginning of the procedure	
Exploration Lesseps (February 1999)	Mining exploration and development	Bankruptcy underway	NA	
Companies whose files are closed, with failure code				
TMI.Education (July 2001)	Computer training and information technologies	9 months	150 people	There was disagreement between management and shareholders
Protec (September 2000)	Information technologies	24 months	Approximately 50 employees	Four-month delay between resolution of the board of directors and the date the notice of intention was filed
Companies that abandoned the procedure before the proposal was accepted by the court				
LBL Skysystems (November 2002)	Engineering, manufacture and installation of window systems and curtain walls	Ongoing (for 34 months)	425	By filing a proposal announcing a proposal amended to a later date, and by obtaining adjournments of the meeting of creditors, the debtor was able to exceed by about two years the maximum time allowed by the BIA between the filing of the notice of intention and presentation of the proposal
Naya (December 1999)	Water bottling	7 months	From 400 in May 1999 to 150 the following December	
Ultravision (July 2002)	Manufacture of corneal lenses and research activities	2 months	150 one year before the beginning of BIA procedures	

Avantage Link	Information technologies	1 month	NA	Questionable transactions by the founding shareholder before the beginning of the BIA procedures drew the attention of the media
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Table 2
Causes of difficulties

Companies that successfully completed BIA procedures	
Bridgepoint	<ul style="list-style-type: none"> • Events of September 11, 2001 • Slowdown in the communications industry • Fixed costs difficult to support, never attained profitability • Parent company no longer able to finance the debtor's losses
Ressources MSV	<ul style="list-style-type: none"> • Major financial losses over the last five years • Low market prices for copper and gold • Depletion of mining resources
Sofame	<ul style="list-style-type: none"> • Implementation of a market plan that happened too slowly • Inadequate cash holdings
Companies whose files are ongoing, without failure code	
Cenosis	<ul style="list-style-type: none"> • Losses of \$7M over the financial year preceding the procedures
CQI Biomed	<ul style="list-style-type: none"> • Death of the founding president • The next president discovered that "the company's finances were in a lamentable state"
Companies whose files are ongoing, with failure code	
Environair Sipa	<ul style="list-style-type: none"> • Insufficient development of sales markets • Insufficient level of commercial activities to support high salaries
Exploration Lesseps	<ul style="list-style-type: none"> • Inadequate financing attributable to the failure to raise public funds
Companies whose files are closed, with failure code	
TMI.Education ⁸	<ul style="list-style-type: none"> • Difficulties of the parent company • Competitors who became shareholders • Financing difficulties
Protec	<ul style="list-style-type: none"> • Losses of more than \$2.7M, leading to a lack of cash holdings • Delay in the development of new products
Companies that abandoned the procedure before the proposal was approved by the court	
LBL Skysystems ⁹	<ul style="list-style-type: none"> • Economic slowdown in the United States • Variances between negotiated prices and real costs
Naya ¹⁰	<ul style="list-style-type: none"> • Loss of American distributor
Ultravision	<ul style="list-style-type: none"> • Implementation of a new sales structure • Serious difficulties at the production level
Avantage Link	<ul style="list-style-type: none"> • Lack of cash holdings • Difficulty in finding new financing due to a class action on the part of the shareholders against a group with which the debtor is affiliated

8. According to the press kit, because the trustee's reports we consulted contained no information on the subject.

9. According to the press kit, because the trustee's reports we consulted contained no information on the subject.

10. According to the press kit, because the trustee's reports we consulted contained no information on the subject.

Table 3
Terms of the proposal

Nature of the proposal	Financing	Presence of inspectors	Anticipated time for payment	Eligible for CCAA	
Businesses that successfully completed BIA procedures					
Bridgepoint	Ordered liquidation of assets	Product of the sale of assets and financing from debtor-operator	1	No time mentioned	Yes
Ressources MSV	New investor in a new entity	<ul style="list-style-type: none"> • Part (\$5M) of the product of the sale of mining assets • Conversion of claims to shares 	5 maximum	20 days	Yes
Sofame	Maintaining ownership rights in assets	Not mentioned in the file	3	\$150,000 when the plan is approved and the balance in 6 months	No
Businesses whose files are ongoing, without failure code					
Cenosis	Continuation of activities	Distribution of the company's shares (no disbursement required)	1	NA	No
CQI Biomed	Realization of assets in a network	<ul style="list-style-type: none"> • A numbered company • Earnings from the five subsequent years 	3	<ul style="list-style-type: none"> • \$25,000 in 30 days • \$150,000 in 5 years 	No
Businesses whose files are ongoing, with failure code					
Environair Sipa	Liquidation	Product of the sale of assets	NA	None	No
Exploration Lesseps	Maintaining ownership rights in assets	Distribution of the company's shares (no disbursement required) and collection of the Crown's claims	5	Two months	No
Table 3					
Nature of the proposal	Financing	Presence of inspectors	Anticipated time for payment	Eligible for CCAA	

Nature of the proposal	Financing	Presence of inspectors	Anticipated time for payment	Eligible for CCAA	
Businesses whose files are closed, with failure code					
TMI.Education	Continuation of activities	Distribution of the company's shares and new financing	NA	30 days	Yes
Protec	Liquidation	An eventual buyer	0	90 days for ordinary claims of \$1,000 or less. 6 months for ordinary claims of more than \$1,000	No
Businesses that abandoned the procedure before the proposal was accepted by the court					
LBL Skysystems	Liquidation	Product of the liquidation	N/A because the creditors ended up rejecting the proposal	NA	Yes
Naya	Liquidation	Product of the liquidation	N/A because the proposal was rejected	As soon as the net product of the sale and the unsecured claims were determined	Yes
Ultravision ¹¹					Yes
Avantage Link ¹²					No

11. The company did not file a proposal with its creditors.

12. The company did not file a proposal with its creditors.

Table 4
The results of creditors' voting

	Ordinary creditors		Trustee's recommendation
	% in number	% in value	
Businesses that successfully completed the BIA procedures			
Bridgepoint	100.0	100.0	Accept
Ressources MSV	100.0	100.0	Accept
Sofame	NA	NA	Accept
Businesses whose files are ongoing, without failure code			
Cenosis	100.0	100.0	Accept
CQI Biomed	92.5	95.8	NA
Businesses whose files are ongoing, with failure code			
Environair Sipa	100.0	100.0	Favourable
Exploration Lesseps	84.6	70.9	Accept
Businesses whose files are closed, with failure code			
TMI.Education	NA	NA	NA
Protec	92.3	76.7	Accept
Businesses that abandoned the procedure before the proposal was approved by the court			
LBL Skysystems ¹³			NA
Naya	77.6	51.3	Reject
Ultravision ¹⁴			
Avantage Link ¹⁵			

13. The meeting of creditors begun in May 2003 has been adjourned three times so far.

14. Because the company did not file a proposal, there was no vote by creditors.

15. Because the company did not file a proposal, there was no vote by creditors.

Table 5
The results of the procedure

	Total receipts (in dollars)	Proven claims (in dollars)	% of write-off – secured claims	% of write-off – ordinary claims	Trustees fees/ Total receipts
Companies that successfully completed the BIA procedures					
Bridgepoint	\$754,713	\$9,159,608, of which \$59,470 in secured claims	44.5	92.8	3.3%
Ressources MSV	\$5,006,563	\$10,510,773	38.9	92.0	0.6%
Sofame	\$304,814	\$970,189	5.0	64.4	NA
Companies whose files are ongoing, without failure code					
Cenosis	NA ¹⁶	\$2,702,290, of which \$901,831 in secured claims	NA	Minimum anticipated of 90%	NA
CQI Biomed	NA ¹⁷	NA	NA	NA	NA
Companies whose files are ongoing, with failure code					
Environair Sipa	\$60,500	\$1,915,421 of which approximately \$220,000 in secured claims	90.8	100.0	Fees for proposal and bankruptcy of about \$30,000
Exploration Lesseps	NA ¹⁸	NA	NA	NA	NA
Companies whose files are closed, with failure code					
TMI.Education ¹⁹	NA	A little over \$4.55M, of which \$1.49M in secured claims	NA	NA	NA
Protec	\$52,276	A little over \$7M, of which \$2.35M in secured claims	NA	99.4 %	41.7 %
Companies that abandoned the procedure before the proposal was approved by the court					
LBL Skysystems	N/A	\$37.1M, of which \$20.5M in secured claims	N/A	N/A	N/A
Naya	N/A	\$98.86M, of which \$77.15M in secured claims	N/A	Estimated at 100%	N/A
Ultravision	N/A	\$19.83M, of which \$13M in	N/A	N/A	N/A

16. As of April 2005, the trustee had not yet filed the final statement of receipts and disbursements or the final dividend sheet.

17. As of April 2005, the trustee had not filed the final statement of receipts and disbursements or the final dividend sheet.

18. The company having failed to implement its proposal, it is deemed to have assigned its property. The file consulted does not contain the final statement of receipts and disbursements, or the final dividend sheet.

19. On December 21, 2001, the day on which the company filed its plan, it transferred its file from BIA to CCAA.

	Total receipts (in dollars)	Proven claims (in dollars)	% of write-off – secured claims	% of write-off – ordinary claims	Trustees fees/ Total receipts
Avantage Link	N/A	secured claims \$1.59M, of which \$0.5M in secured claims	N/A	N/A	N/A

Table 6
Quality and quantity of information available

Info on the rejection scenario		Other
Businesses that successfully completed the BIA procedures		
Bridgepoint	Limited to mentioning that in the event of bankruptcy, the related claims would not be reduced by 20%, which would probably eliminate any possible recuperation for the other ordinary creditors.	<ul style="list-style-type: none"> Sales do not decline immediately after September 11, 2001
Ressources MSV	Limited to mentioning that based on experience and an assessment by a firm of experts, no dividends would be paid out in the event of bankruptcy	<ul style="list-style-type: none"> Coherence between the cause of the difficulties identified and the financial statements preceding the date of the notice of intention The previous statements show significant capitalization of exploration costs (about \$6M) Despite its difficulties, the company long succeeded in attracting investors
Sofame	In a bankruptcy context, the dividend is estimated at 30%, while the trustee estimates the dividend resulting from the proposal at 35%	<ul style="list-style-type: none"> Transfers between the parent company and its subsidiaries make it difficult to assess the completeness of the assets and the reliability of the results
Companies whose files are ongoing, without failure code		
Cenosis	Limited to mentioning that no dividends could be expected in the event of bankruptcy	<ul style="list-style-type: none"> The deficit projected in the cash-flow statement (CFS) is not commented on, despite a request for an extension
CQI Biomed	Limited to stating that since ...fiscal losses could never be recovered in the event of bankruptcy, it is certain that creditors would not receive any dividends.	
Companies whose files are ongoing, with failure code		
Environair Sipa	Limited to mentioning that there would be a lower dividend in the event of bankruptcy	<ul style="list-style-type: none"> This file raises a lot of questions as to the completeness of the assets
Exploration Lesseps	Dividend would be lower in the event of bankruptcy	<ul style="list-style-type: none"> Significant capitalization of exploration costs Some assets seem to have disappeared before the date of the proposal

	Info on the rejection scenario	Other
Companies whose files are closed, with failure code		
TMI.Education	Limited to mentioning that unsecured creditors would not receive any dividends in the event of bankruptcy	<ul style="list-style-type: none"> • The deficit projected in the cash-flow statement is not commented on, despite a request for an extension • The company is part of a group that frequently concludes purchase or sale operations of member companies
Protec	Limited to mentioning that, in the event of bankruptcy, the balance available for dividends to unsecured creditors would be zero	<ul style="list-style-type: none"> • It is possible that in 1999, management chose accounting arrangements that allowed it to reduce the figure of the net income accountable
Companies that abandoned the procedure before the proposal was approved by the court		
LBL Skysystems	Limited to mentioning that, in the event of bankruptcy, it is unlikely that unsecured creditors will receive any dividends	<ul style="list-style-type: none"> • The trustee's reports contain a great deal of financial information
Naya	No comments to this effect, probably because of the amount by which secured claims exceed the negotiated price for the sale of the debtor's assets	<ul style="list-style-type: none"> • The deficits projected in the cash-flow statement are not commented on, despite the requests for extension
Ultravision		<ul style="list-style-type: none"> • Given that there was no proposal filed, there was for all practical purposes no information made available to unsecured creditors before the debtor's bankruptcy
Avantage Link		<ul style="list-style-type: none"> • Doubtful reliability of the financial statements due to frequent changes in auditors and corrections made to past financial years

Appendix A

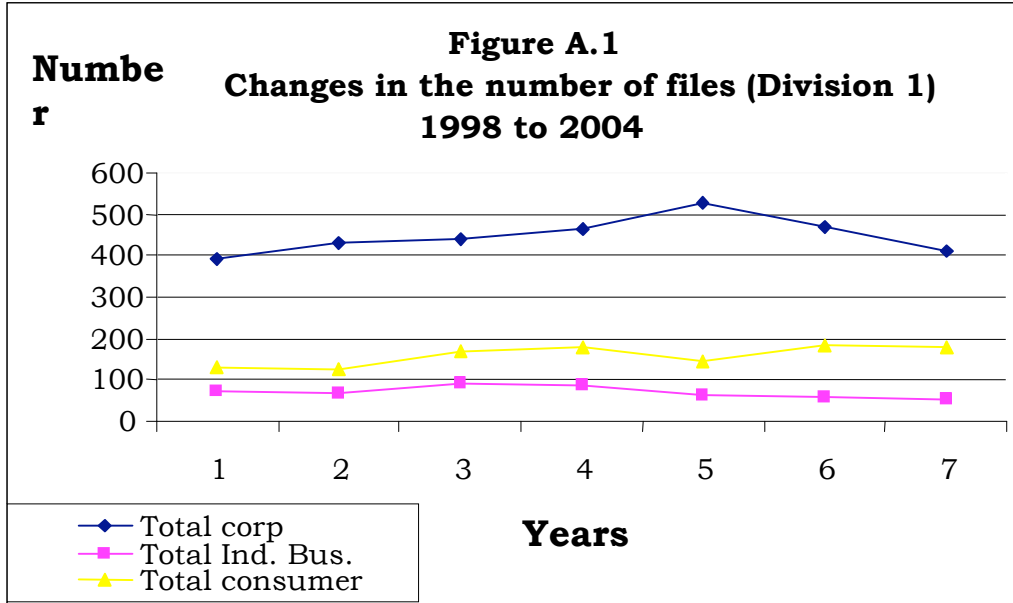
Characteristics of the use of reorganization procedures under the BIA by incorporated businesses Province of Quebec

A – The empirical scope of the research: incorporated businesses¹

The statistics on proposals published by the Office of the Superintendent reflect the distinction made in the BIA between consumer proposals (Division II proposals, in reference to Division II in Part III of the Act) and proposals in general (Division I proposals). Division II proposals are those made by or for a natural person who is bankrupt or insolvent and whose aggregate debts, excluding any debts secured by the person's principal residence, do not exceed seventy-five thousand dollars. Division I proposals include all other proposals; the statistics organize them into three groups: consumers, individual businesses, and incorporated businesses.

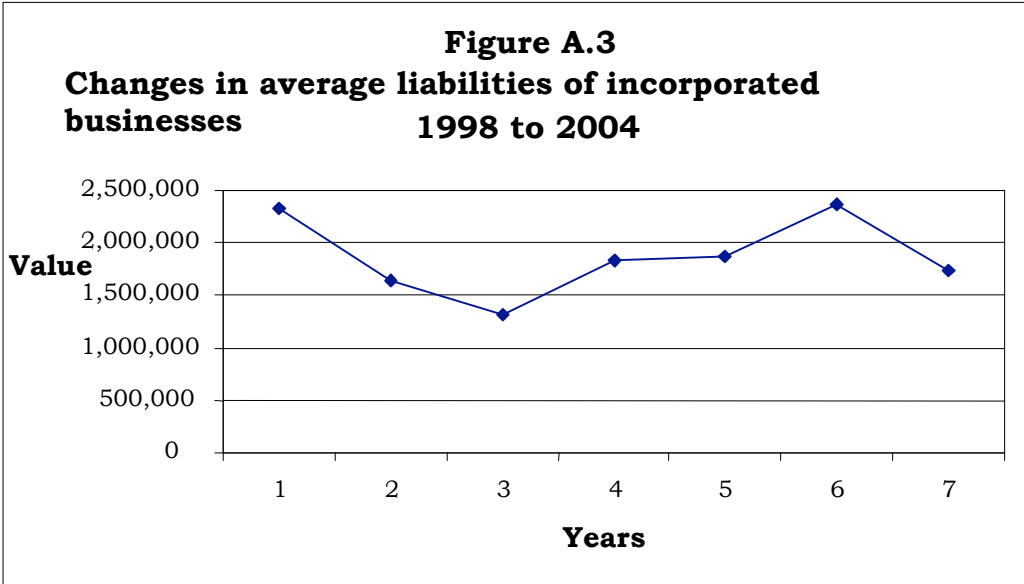
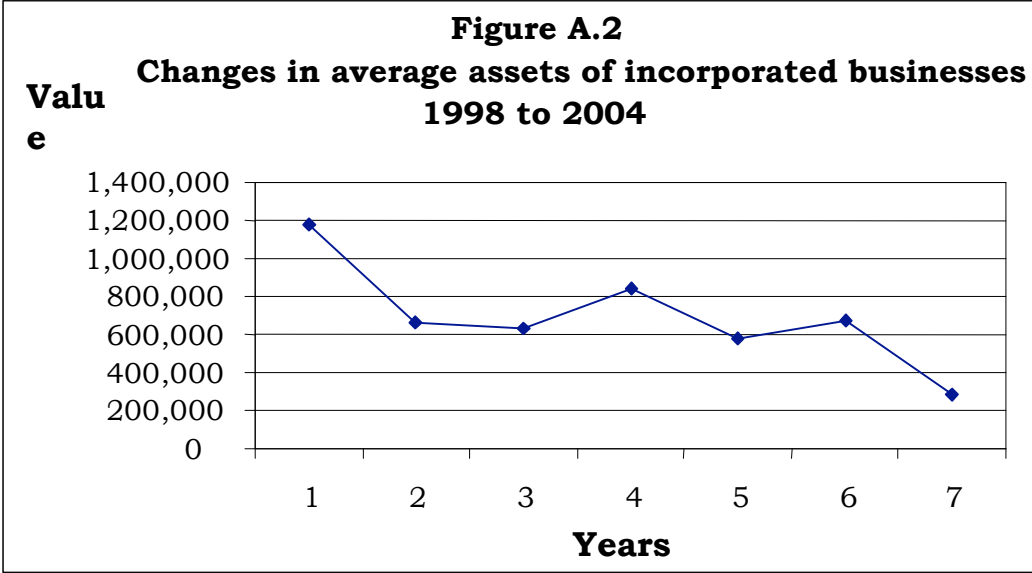
For the period analyzed (1998-2004), there were, on average, nearly ten times more proposals for incorporated businesses than for individual businesses (Figure A.1). This is one of the reasons for focusing this research on incorporated businesses. Other reasons for this choice include first of all the fact that the amount of assets is on average several times higher for reorganizations of incorporated businesses than for individual businesses. Secondly, the reliability of accounting data for companies, particularly with regard to the separation between the personal financial situation of managers and the financial situation of the company, tends to increase with the size of the company. Thirdly, given that with Division I proposals the criterion for distinguishing between the "consumers" category and the "individual businesses" category is based on the amount of the insolvent entrepreneur's business debts relative to personal debts, the accounting data for a number of individual businesses do not deal exclusively with the "business" element of the proposal. Considering that the central theme of the research is the management of businesses' accounting and financial information in the context of company reorganizations, all of these reasons justify concentrating the empirical research on proposals for incorporated businesses.

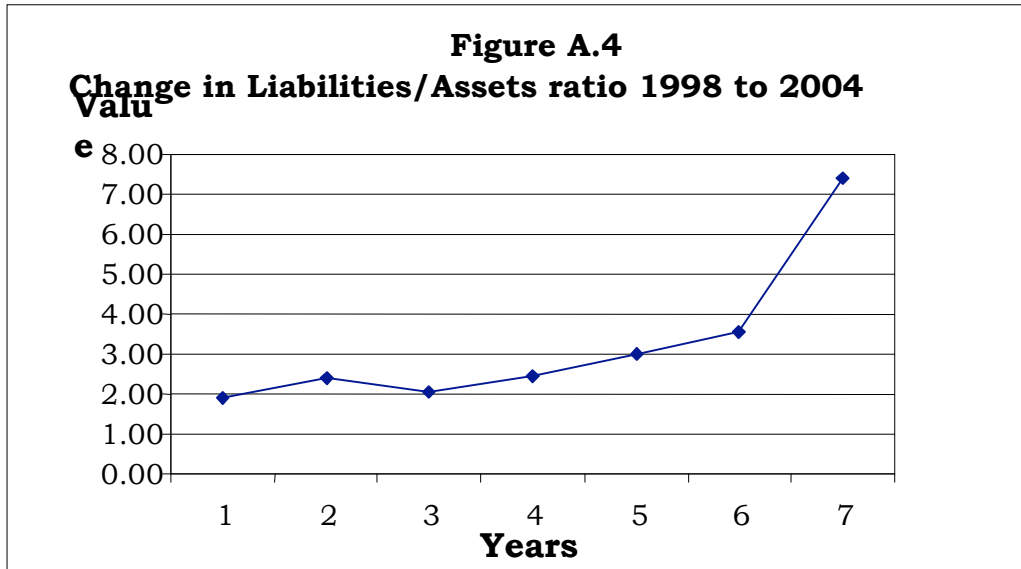
1. In this appendix, "company" and "incorporated business" are used as synonyms.



B – Changes in amount and level of indebtedness

Figure A.2 shows that the average assets of corporations undertaking reorganization procedures pursuant to the BIA varied significantly, tending towards decreases at the beginning and end of the period in question. Figure A.3 shows that average liabilities also varied significantly over the same period, but without a trend toward decreases. It follows, as indicated by Figure A.4, that the Liabilities/Assets ratio also varied over the period, with an appreciable upwards trend at the end. Various theories might explain this evolution toward a lower coverage of liabilities. It may be that creditors, or certain classes of them, extended credit more and more easily over that period, thereby enabling companies in difficulty to accumulate more debt. A second possibility, which does not exclude the first, is that companies in difficulty were taking longer and longer to avail themselves of reorganization procedures.





C – Montréal region versus the rest of the province

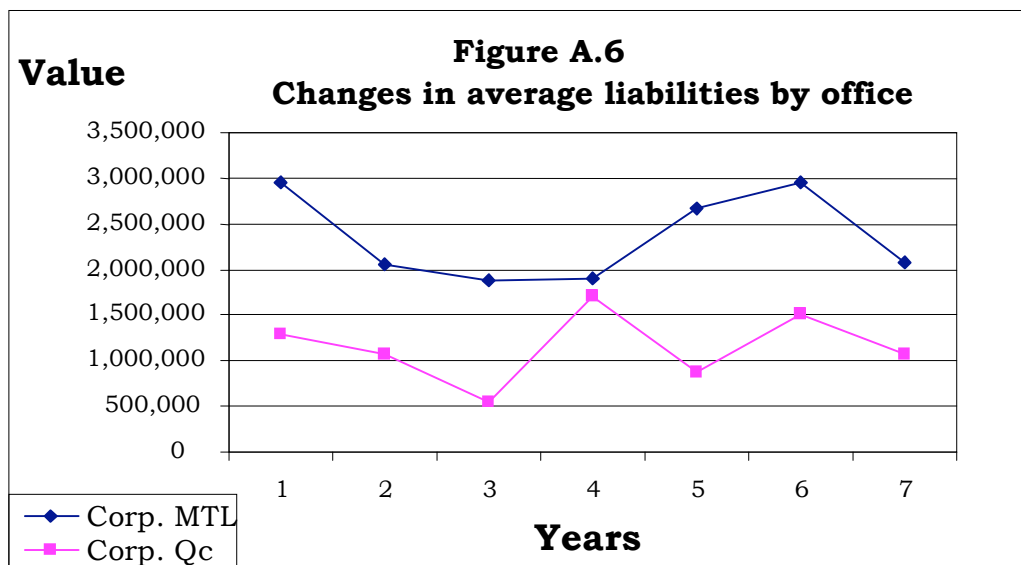
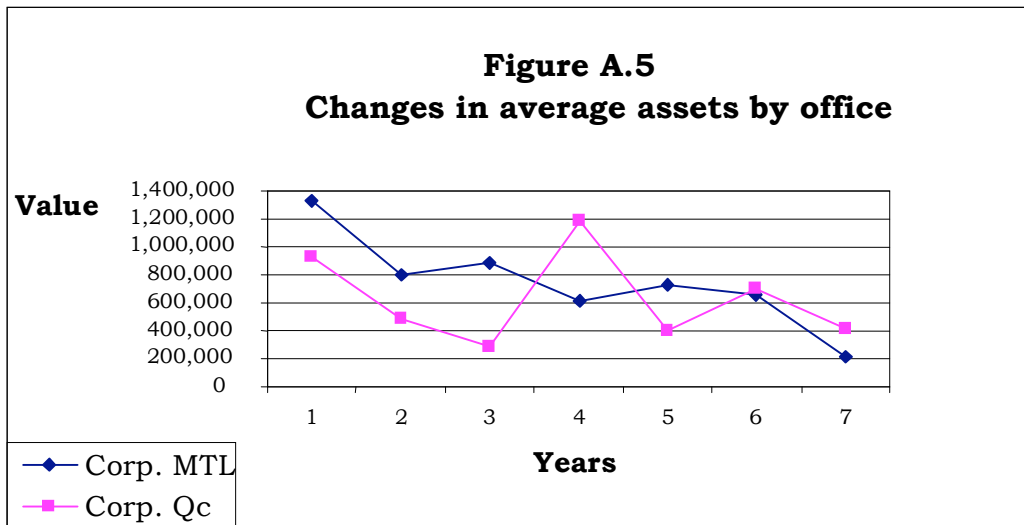
The overall data for the Province of Quebec reported in Figures A.1 to A.4 come from the Superintendent's two regional offices in Montréal and Ste-Foy (Québec City). Significant differences can be observed in proposals presented at each of these offices. First, as indicated by Table A.1, the ratio of the number of incorporated businesses to the number of individual businesses undertaking reorganization procedures is much lower for proposals filed in the Ste-Foy office than for proposals filed in the Montréal office.

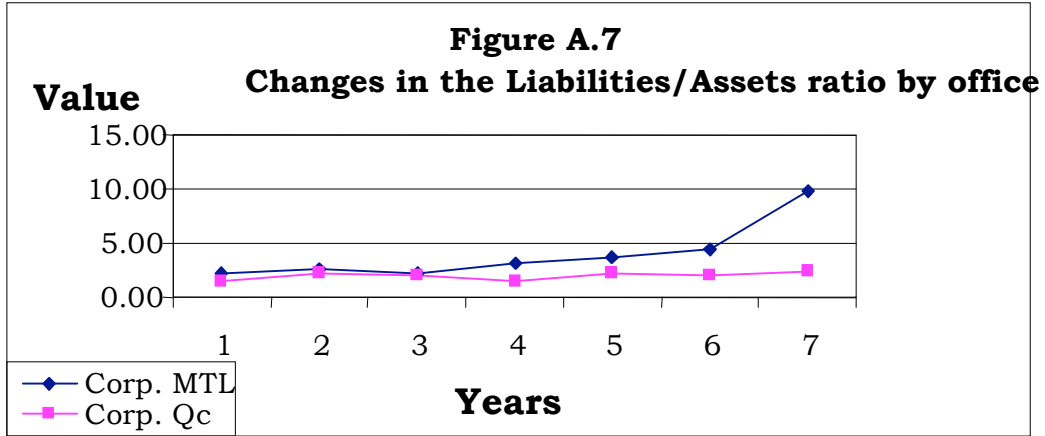
Table A.1
Businesses commencing reorganization procedures:
number of incorporated businesses / number of individual businesses

	Ste-Foy	Montréal
1998	1.79	10.25
1999	4.07	9.92
2000	3.44	6.54
2001	3.17	9.82
2002	5.69	14.4
2003	6.00	10.26
2004	4.09	13.65

Secondly, the average amount of assets and liabilities and the changes in those amounts over the period are very different from one office to the other, as indicated in Figures A.5 and A.6. These differences lead to a Liabilities/Assets ratio that is systematically higher for proposals in the Montréal office (Figure A.7). It will be interesting to see, using data on

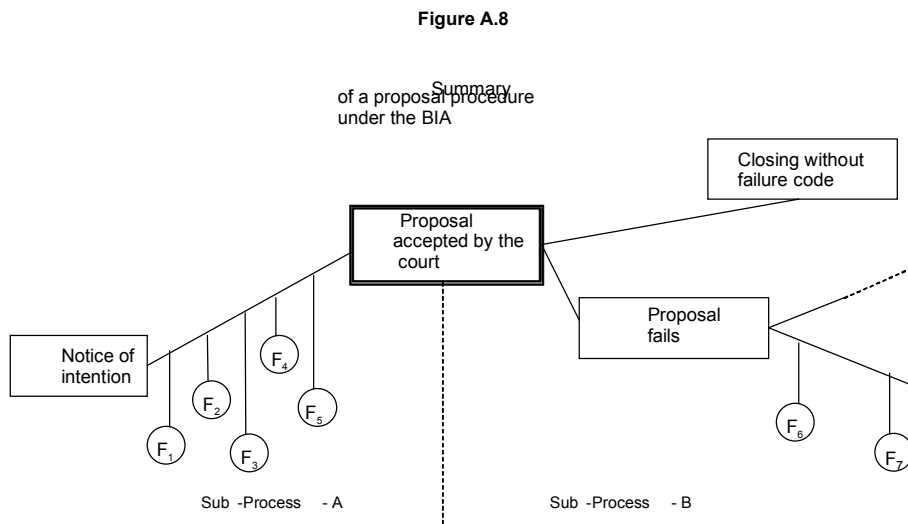
dividends, whether this leads to decreased losses on average for the creditors involved in the proposals presented to the Ste-Foy office. And what would explain that the Liabilities/Assets ratio is substantially higher for proposals filed in the Montréal office in 2004? It may be that the theories put forth in the previous section are more applicable to the Montréal region or, similarly, that there is less rationing of credit for companies located in major centres. This could translate, among other things, into a higher Liabilities/Assets ratio at the time of insolvency.





D – Stages in the reorganization process

Access to reorganization procedures under the BIA is relatively easy. The company retains a trustee to perform a basic assessment of the insolvency situation and then file with the Office of the Superintendent of Bankruptcy a notice of intention to make a proposal. This notice triggers a process that will, ideally, lead to approval of a proposal by the creditors and the court. Court approval is a pivotal point in the BIA reorganization procedure; once the debtor company has attained that approval, it is granted new life in the sense that the threat of imminent action by creditors to seize its assets is put off for some time. The degree of this new autonomy is determined by the terms of the proposal. Figure A.8 provides an overview of a BIA reorganization procedure. Here, the procedure is divided into two sub-processes, one on either side of the crucial stage of court approval of the proposal.

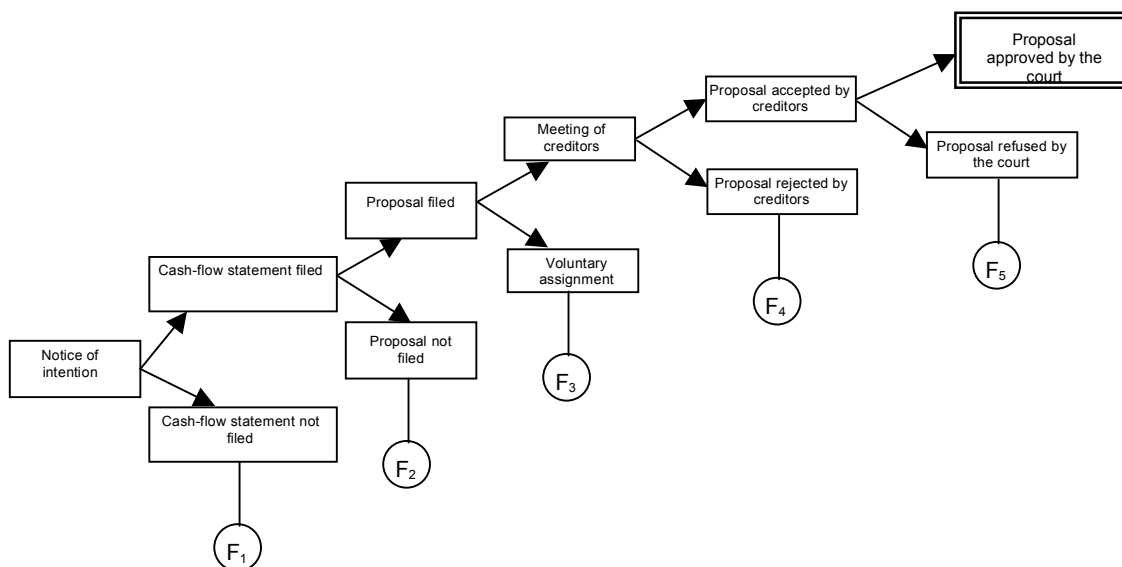


Note: The Fs represent the seven possibilities for applying bankruptcy procedures (termination or bankruptcy order) during a proposal procedure under the BIA.

Once the proposal is accepted by the court, i.e., under Sub-process B, there are two possible outcomes. If the proposal is performed to the satisfaction of the parties involved, the trustee will be discharged and the file will be closed without notice of default being filed with the OSB. On the other hand, if one or more of the terms of the proposal are not respected, the proposal is considered to have failed, and depending on the will of the parties involved, this could lead to the company's bankruptcy. Figure A.8 illustrates these two possible outcomes.

Prior to court approval of the proposal, i.e., under Sub-process A in Figure A-8, the procedure provides for a schedule of conditions accompanied by time lines. If the company is not able to meet these conditions, it will be deemed to have assigned its property within the meaning of the BIA and will therefore be in bankruptcy. Figure A.8 suggests five scenarios that could lead to the bankruptcy of a debtor company, of which four can be seen as mechanisms for controlling the debtor company that has chosen to undertake a proposal procedure. Figure A.9 identifies these five scenarios.

Figure A.9
Diagram of the BIA proposal procedure up to court approval of the proposal (sub-process A)



Note : F₁ to F₅ represent the five possible interruptions of the procedure that imply bankruptcy.

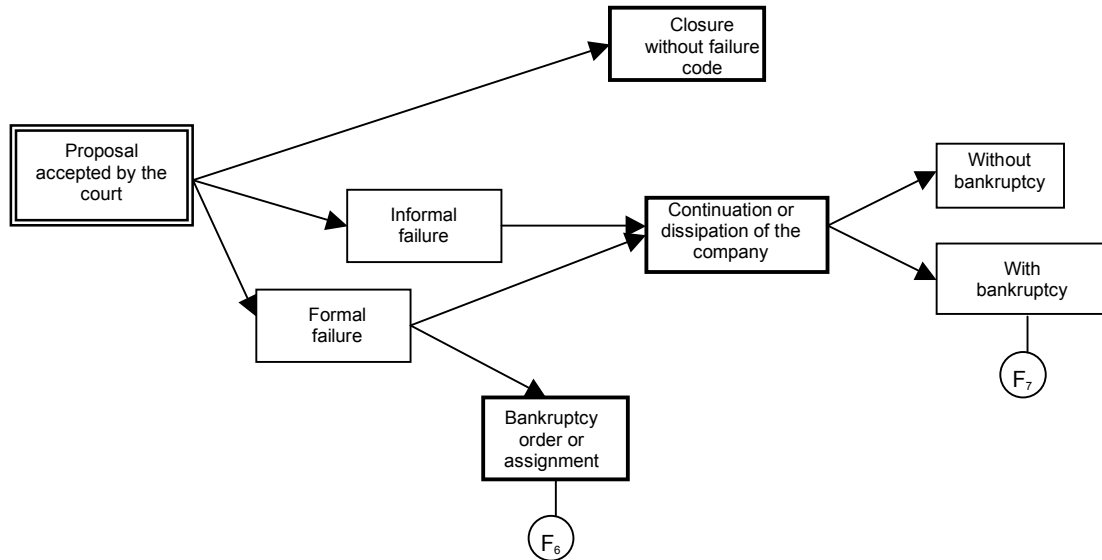
F3 in Figure A.9 represents a voluntary assignment by the debtor company's management. It was placed in the middle of the diagram but could happen at any point; once the company is deemed insolvent, its management can make a voluntary assignment at any time. The four other situations represented respectively by F1, F2, F4 and F5, constitute mechanisms for controlling the debtor company making use of the reorganization procedure. In F1, the company is deemed to have made a voluntary assignment because it did not present its cash-flow statement for the current and upcoming periods within ten days of filing its notice of intention. In F2, the company is deemed to have made a voluntary assignment because it did not file its proposal within thirty days of filing the notice of intention, or before the end of the additional period approved by the court for presenting a proposal. The Act allows the court to accord a maximum of three additional extensions of 45 days each, if it is presented with valid justification. In F4, the company is deemed to have made a voluntary assignment because the proposal it filed is rejected by the creditors. In F5, the company is deemed to have made a voluntary assignment because the proposal, while accepted by the meeting of creditors, is rejected by the court.

The trustee filing the notice of intention plays an important role in the various stages of the procedure; for example, it is to the trustee that the company must submit its cash-flow statement. In a number of ways, the trustee acts as an officer of the court with access to the books of the debtor company.

Figures A.10 and A.11 present a little more detail on Sub-process B, i.e., the stages of the procedure once the proposal is accepted by the court. For purposes of Figure A.10, which explicitly identifies the two bankruptcy scenarios for a debtor company in Sub-process B, we assumed that the files of all companies for which there had been a notice of intention have been closed, i.e., that the procedure has been terminated. This allowed us to illustrate all the possible scenarios for companies whose proposals have been accepted by the court. If all terms and conditions of the proposal are performed to the satisfaction of the creditors or the committee of appointed inspectors, no notice of default will be issued by the trustee, and

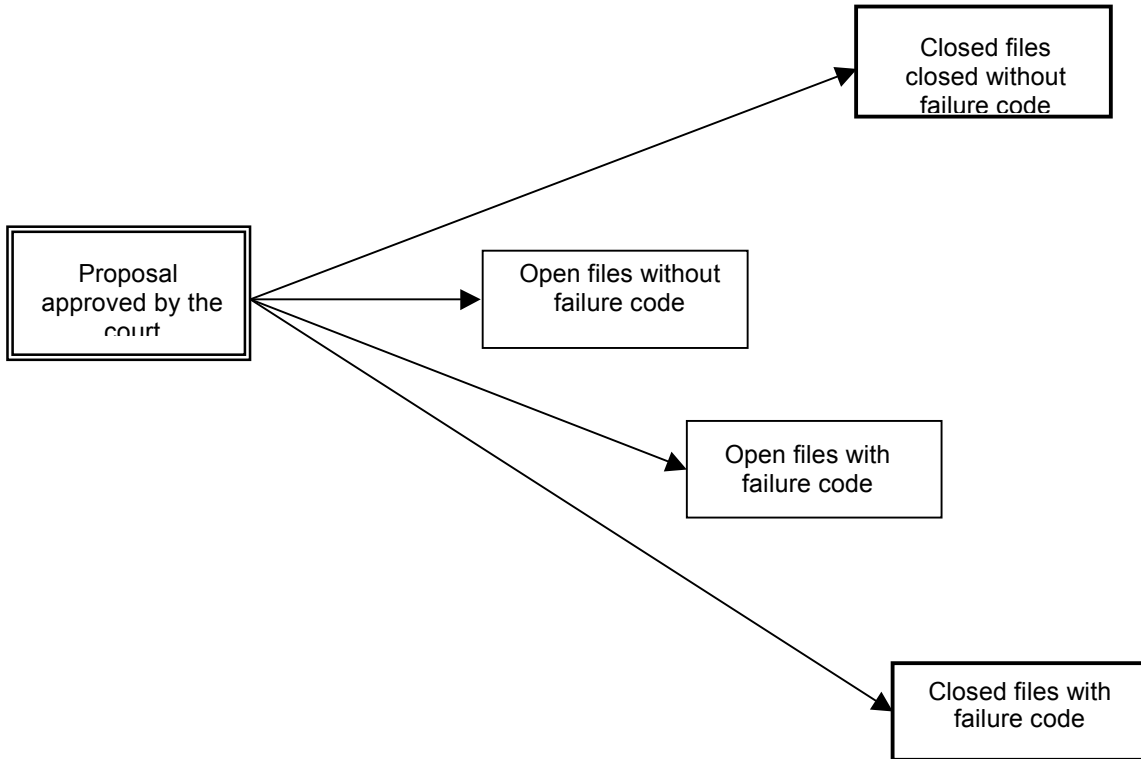
therefore no failure code will appear on the company's file. After approval of his or her final statement of receipts and disbursements, the trustee will be discharged and the file closed.

Figure A.10
Diagram of the proposal procedure after court approval of the plan (Sub-process B)
Assumption: all files are closed



Note : F₆ and F₇ represent the two possible interruptions in the implementation of the proposal or application of bankruptcy procedures in Sub-process B.

Figure A.11
 Diagram of the proposal procedure after court approval of the
 proposal
 Actual file at a specific date



However, if some terms or conditions included in the proposal are not respected, and the committee of inspectors does not feel it appropriate, or does not have the authority to relax the terms of the proposal in this area, the trustee will file a notice of default. This becomes a formal failure. But the company's bankruptcy is not automatic. Someone must be prepared to assume the costs of a bankruptcy procedure. Figure A.10 presents this scenario in F6. There is also the possibility of a less formal failure with complete, or almost complete, dissipation of the debtor company's assets and a procedure that drags on longer without notice of default being filed. Another possibility is that after a certain amount of time, one of the parties still involved triggers bankruptcy proceedings before a notice of default has been filed. This scenario is set out in F7 of Figure A.10. Figure A.11 completes Figure A.10 in anticipation of the statistical tables in the next sections; it identifies the four categories of company for which a proposal has been accepted.

E. Degree of success based on the stage reached in the procedure²

The proportion of companies for which the procedure was successfully completed – and among those for which this was not the case, the stage reached in the procedure – constitutes an important indicator of the use and implementation of the Act. A pivotal point in the procedure is the stage at which the proposal is accepted by the court. This stage in some ways gives new life or new autonomy to the company as compared with its initial state of

2. The following tables are all grouped together at the end of this Appendix.

insolvency. The level of success will therefore be measured after court approval, while in the event of failure, the stage reached in the process will be sometime before court approval.

Table A.2 provides the breakdown in the percentage of cases based on the stage reached in the procedure up to approval of the proposal by the court. For the period 1998-2003, a little under half (47.9%) of the 2,704 files of incorporated businesses for which a notice of intention was filed in the Province of Quebec gave rise to the filing of a proposal approved by the court. There is a slight difference between the Québec City and Montréal offices: for the latter, the percentage decreases to below 45%, while the percentage for the former exceeds 50%. The most significant reduction in percentage points among the different stages before court approval is found between the filing of the cash-flow statement (CFS) and the filing of the proposal; about one fifth of incorporated businesses that file a notice of intention do not actually file a proposal. The experience is very similar in Québec City and Montréal. The difference between the two cities mentioned previously is principally due to the higher rate of rejection by creditors of proposals filed in Montréal than in Québec City: a little less than 10% of the total number of notices of intention for Québec City, and more than 15% for Montréal.

Tables A.3 and A.4 present the percentage distributions for Table A.2 for Montréal and Québec City and by year they were opened. The annual variations do not suggest a particular trend over the period, aside from a rejection rate by creditors in Montréal that was slightly higher from 2000 on than it was in the 90s.

Table A.5 indicates the percentage breakdown of proposals approved by the court based on the results of the proposals: confirmed success or formal failure. Confirmed success is defined as a closed file without failure code, while formal failure corresponds to a file in which the trustee issued a notice of default or in which there was bankruptcy. Approximately one quarter of proposals approved by the court are failures as defined here. This measure is specific to the period under observation, which fact is particularly important for “younger” files, and those for which court approval of the proposal took place near the end of the period. This figure increases by about one third for filings in the Montréal office, and decreases by about one fifth for filings in the Québec City office.

Tables A.6 and A.7 present the percentage distributions for Table A.5 for Montréal and Québec City and by year of opening. For both cities, there is an observed increase over this period in the percentage of files without formal failure, and a decrease over the period in the percentage of files closed without a failure code. As previously emphasized, these changes are explained in part, if not in whole, by the age of the files. As we approach the end of the period, the age of files decreases steadily. This can affect the percentages in two ways. First, performance of the proposal being observed over a shorter period, the probability of failure is lower. Secondly, to the extent that files that pass through the entire procedure more quickly generally have a lower rate of failure, a shorter period of observation implicitly deals with a larger proportion of successful files.

F. Defining a global measure: indicator of the average stage reached

It is reasonable to assume that some aspects of a company's operations could affect the degree of success of a reorganization procedure. Among the possible differentiation circumstances affecting companies' experiences with the reorganization procedure are those that tend to affect companies differently based on their area of activity. Cost structures and resale values of production and other goods can also constitute differentiation circumstances. These circumstances being specific to each sector, one way to verify whether they are determinant in a company's experience with the BIA reorganization procedure would be to calculate some of the distributions reported in the preceding tables for specific sectors of activity.

Besides the sector, the region, as suggested by some of the preceding tables, as well as the year and other variables such as the amount of assets held by a company can affect the degree of success of a reorganization procedure. In the context of an exploratory study of the factors of differentiation in the degree of success of a reorganization procedure, it would be useful to have a global measure or indicator of the average stage reached in the procedure by various sub-groups of companies classified by specific characteristics. To this end, the various scenarios that could give rise to bankruptcy before the stage where the proposal is accepted by the court were all given a number between 0 and 4. Given that the debtor company can proceed to a voluntary assignment at any time within Sub-process A, the median value of 2 represents voluntary assignments.

Files that have passed through the stage of court approval of the proposal and have a failure code in the Superintendent's files were given a value of 5. Files that passed through this same stage and were closed without a failure code over the period 1998-2003 received a value of 6. The coding of still-open files that moved beyond the stage of court approval of the proposal and don't have a failure code requires making certain assumptions with regard to their future evolution. To this end, the coding distinguished between two scenarios: a pessimistic one and an optimistic one. For the pessimistic scenario, files received a value of 5, in anticipation of an eventual failure code. In the optimistic scenario, files were given a value of 6, in anticipation of the eventual closing of the file without a failure code. Table A.8 presents the values by stage.

For each sub-group of files, each scenario gave rise to a calculation of the first indicator of the average stage reached, qualified as optimistic, and a second indicator of the average stage reached which is pessimistic; the value of an indicator corresponding to the simple mathematical average of the values assigned to the files in the sub-group. The pessimistic and optimistic indicators for a sub-group can be interpreted as the lower and higher boundaries of the definitive value of the indicator for the average stage reached when all the files in the sub-group have been closed. Table A.9 presents the values of the pessimistic and optimistic indicators for all files in the Province of Quebec over the period 1998-2003, as well as for the sub-groups of Montréal and Québec City files. For the province, the definitive value of the indicator comes in at around 3.6. Considering the values allocated, this means that on average, the stage reached by files is between the stage where the proposal is accepted by the creditors and the stage where it is approved by the court. The values of the indicators for Montréal and Québec City confirm the preceding observations on the percentage distributions: the value of the indicator for the average stage reached for the sub-group of Québec City files is higher than the value of the indicator of the average stage reached for the sub-group of Montréal files.

Table A.10 shows the indicator values, based on the optimistic scenario, on an annual basis and distinguishing between Montréal and Québec City files. With the exception of 2001, on average Québec City files went further in the procedure than Montréal files. Table A.11 reports on the indicator values for each of the scenarios for the sub-groups of companies classified by sector of activity. We can observe some significant variations between sectors. For example, the indicator values based on the optimistic scenario range from a minimum of

3.13 for the Retail sector to a maximum of 4.17 for the Primary sector (agriculture, forestry, ...).

G. Sectoral and regional differences

The sectoral distribution of economic activity is not uniform across regions. The Québec City office has a higher proportion of companies that operate far from major centres, while the Montréal office has a higher proportion of companies located in or just outside a major centre. For example, holding proportions constant, the Manufacturing Sector and the Business Services sector are relatively more important in a major centre or just outside a major sector than the same sectors in regions far removed from major centres. The observations presented in the previous sections raise the question as to whether the differences between Québec City and Montréal are due to variations in the sectoral composition of economic activity in the two regions. Tables A.12 and A.13 offer a first response to that question. Even after having corrected for the sector, i.e., keeping the sector constant, the average stage reached for Québec City files is higher for all sectors, except for one of marginal significance in the database (Health Services).

Tables A.14 to A.21 demonstrate the average stage reached in the procedure for Québec City office files and those for the Montréal office by year for the eight most important sectors of the ten in Tables A.12 and A.13. The eight sectors for the six years give forty-eight observations on the Québec City – Montréal differences. For thirty-two of these forty-eight observations, the Québec City files reached a higher average stage within the procedure.

H. Assets, liabilities and length of the procedure

Exploratory research such as that which preceded this calculation of percentages and indicators is intended more to identify questions than to test assumptions. Is it possible, for example, that the variations at the sectoral and regional levels are related to, or reflect, the effect of other accounting or financial variables, like the amount of assets or liabilities reported by the debtor company when it initiated the reorganization procedure? Table A.22 presents the values for the optimistic scenario, for Montréal by sector, based on the size of the assets basket reported by the company when it commenced the procedure. For all sectors, the average stage reached in the procedure is significantly higher for companies whose basket of assets is larger than the median than for companies whose basket of assets is smaller than the median.

Table A.23 presents the values of the optimistic indicator, for Montréal by sector, based on the amount of liabilities reported by the company when it commenced the procedure. Contrary to the preceding table, the differences are rarely significant between the two size classes and do not point systematically in one direction or another in all sectors. The interpretation of these results requires more analysis; it is worth noting that the size of the basket of assets or the amount of liabilities do not flow exclusively from the size of the company experiencing financial difficulties, but also reflect, at least in part, the date on which the company initiated a procedure relative to the date on which it began to experience serious difficulties.

Tables A.24 and A.25 use the same calculations as the two preceding tables, but for filings in the Québec City office. For the assets variable, the results are similar, but for the liabilities variable, the average stage reached in Québec City is higher for the majority of sectors in the case of files with liabilities above the median.

Another variable that could affect the average stage reached in the procedure by a group of companies is the length of the procedure, the assumption being that files that move quickly tend to be less problematic. Tables A.26 and A.27 present the average level reached for

Québec City and Montréal based on the number of days of procedure. Generally speaking, the higher the number of days of procedure, the lower the average stage reached.

Table A.2

**Distribution of incorporated businesses that used the BIA
proposal procedure, by stage reached, up to court
approval of the proposal**

1998-2003

	Province	Montréal	Québec City
Number of files	2,704	1,580	1,124
Notice of intention	100%	100%	100%
CFS filed	96.3%	96.5%	96.0%
Proposal filed	77.8%	77.1%	78.7%
Proposal presented to the creditors	62.1%	61.0%	63.5%

Proposal accepted by the creditors	48.7%	44.8%	54.1%
Proposal accepted by the court	47.9%	44.4%	52.8%

Table A.3

**Changes from 1998 to 2003 in the percentage distribution,
by stage reached, up to acceptance of the proposal**

Montréal

	1998	1999	2000	2001	2002	2003
Number of files	246	246	255	274	285	274
Notice of intention	100%	100%	100%	100%	100%	100%
CFS files	93.1%	95.5%	97.3%	97.4%	97.9%	97.4%
Proposal filed	72.4%	74.4%	82.4%	77.7%	77.5%	77.7%
Proposal presented to the creditors	53.7%	58.1%	65.9%	67.5%	59.6%	60.6%

Proposal accepted by the creditors	37.4%	39.4%	46.7%	50.0%	45.6%	48.5%
Proposal accepted by the court	36.6%	39.4%	46.7%	49.6%	44.9%	47.8%

Table A.4

Changes from 1998 to 2003 in the percentage distribution, by stage reached, up to acceptance of the proposal

Québec City

	1998	1999	2000	2001	2002	2003
Number of files	143	183	184	188	237	189
Notice of intention	100%	100%	100%	100%	100%	100%
CFS filed	96.5%	97.3%	98.9%	93.1%	98.7%	91.0%
Proposal filed	78.3%	78.1%	86.4%	73.4%	80.6%	75.1%
Proposal presented to the creditors	58.7%	61.2%	70.1%	56.9%	69.6%	61.9%

Proposal accepted by the creditors	51.0%	54.6%	59.8%	48.4%	55.7%	54.0%
Proposal accepted by the court	50.3%	53.0%	59.2%	46.3%	53.6%	53.4%

Table A.5

**Results of the BIA proposal procedure
where the proposal was accepted by the court**

1998-2003

	Province	Montréal	Québec City
Number of files	1,294	701	593
Proposals accepted by the court	100%	100%	100%
	(47.9)	(44.4)	(52.8)
No formal failure	70.8%	64.2%	78.6%
	(33.9)	(28.5)	(41.5)
Closure without failure code	43.6%	34.5%	54.4%

(20.9)

(15.3)

(28.7)

Note: numbers in brackets represent the number of files as a percentage of the number of notices of intention filed.

Table A.6

**Changes in the results of the proportion of BIA proposals
where the proposal was accepted by the court, 1998 to 2003**

Montréal

	1998	1999	2000	2001	2002	2003
Number of files	90	97	119	136	128	131
Proposals accepted by the court	100%	100%	100%	100%	100%	100%
	(36.6)	(39.4)	(46.7)	(49.6)	(44.9)	(47.8)
No formal failure	60.1%	53.6%	59.5%	64.1%	63.3%	81.0%
	(22.0)	(21.1)	(27.8)	(31.8)	(28.4)	(38.7)
Closure without failure code	47.8%	39.1%	41.1%	39.7%	22.7%	21.3%

(17.5) (15.4) (19.2) (19.7) (10.2) (10.2)

Note: numbers in brackets represent the number of files as a percentage of the number of notices of intention filed.

Table A.7

**Changes in the results of the BIA proposal procedure
where the proposal was accepted by the court, 1998 to 2003**

Québec City











	1998	1999	2000	2001	2002	2003
Number of files	72	97	109	87	127	101
Proposals accepted by the court	100%	100%	100%	100%	100%	100%
	(50.3)	(53.0)	(59.2)	(46.3)	(53.6)	(53.4)
No formal failure	71.0%	76.2%	82.6%	82.7%	75.6%	83.1%
	(35.7)	(40.4)	(48.9)	(38.3)	(40.5)	(44.4)
Closure without failure code	66.8%	66.0%	60.6%	59.8%	47.2%	32.8%

(33.6) (35.0) (35.9) (27.7) (25.3) (17.5)

Note: numbers in brackets represent the number of files as a percentage of the number of notices of intention filed.

Table A.8

**Coding of the various stages of the procedure
for purposes of calculating the indicator of
average stage reached by companies in a group**

	Notice of intention	Code value
	Cash-flow statement not filed	0
	Proposal not filed	1
	Voluntary assignment	2
	Proposal rejected by the creditors	3
	Proposal refused by the court	4
	Proposal approved by the court	
	Files with failure code	5
	Open files without failure code	
	Pessimistic indicator	5
	Optimistic indicator	6
	Closed files without failure code	6

Note: the "Fs" represent possible applications of bankruptcy procedures (see the summary of a proposal procedure – Figure A.8 and the diagram of Sub-process A – Figure A.9.)

Table A.9

**Indicator of the average stage
reached for all files**

1998-2003

	Province	Montréal	Québec City
Pessimistic indicator	3.54	3.39	3.74
Optimistic indicator	3.67	3.52	3.87

Table A.10

**Changes in the annual indicator of the average stage reached,
1998 to 2003, for all files
Optimistic scenario**

Year	Montréal	Québec City	Québec City - Montréal
1998	3.15	3.71	+0.56
1999	3.28	3.85	+0.57
2000	3.67	4.23	+0.56
2001	3.74	3.56	-0.18
2002	3.54	3.99	+0.45
2003	3.71	3.80	+0.09

Table A.11

**Indicator of the average stage reached
by sector based on the pessimistic and optimistic scenarios**

Sector	Optimistic scenario	Pessimistic scenario
Primary (agriculture, forestry, ...)	4.17	4.28
Construction	3.86	4.02
Manufacturing	3.48	3.60
Business services	3.52	3.65
Health services	3.74	3.88
Restaurant and hotel industry	3.57	3.72
Other services	3.54	3.70
Wholesale trade	3.42	3.52
Retail trade	3.13	3.22
Transportation and warehousing	3.77	3.98

Table A.12

**Variations between Montréal and Québec City in sectoral indicators
of the average stage reached
Optimistic scenario
1998 - 2003**

Sector	Montréal	Québec City	Québec City - Montréal
Primary (agriculture, forestry, ...)	3.94	4.38	+0.44
Construction	3.99	4.04	+0.05
Manufacturing	3.46	3.90	+0.44
Business services	3.60	3.75	+0.15
Health services	3.95	3.80	-0.15
Restaurant and hotel industry	3.64	3.82	+0.18
Other services	3.50	3.86	+0.36
Wholesale trade	3.46	3.63	+0.17
Retail trade	2.94	3.61	+0.67

Transportation and warehousing

3.78

4.20

+0.42

Table A.13

**Variations between Montréal and Québec City in sectoral indicators
of the average stage reached
Pessimistic scenario
1998 - 2003**

Sector	Montréal	Québec City	Québec City - Montréal
Primary (agriculture, forestry, ...)	3.88	4.27	+0.39
Construction	3.80	3.92	+0.12
Manufacturing	3.33	3.79	+0.46
Business services	3.46	3.65	+0.19
Health services	3.79	3.67	-0.12
Restaurant and hotel industry	3.50	3.66	+0.16
Other services	3.33	3.73	+0.40
Wholesale trade	3.38	3.49	+0.11
Retail trade	2.88	3.49	+0.61

Transportation and warehousing	3.53	4.04	+0.51
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Table A.14**Changes in the annual indicator of the average stage reached
from 1998 to 2003 for files in the Construction sector****Optimistic scenario**

Year	Montréal	Québec City	Québec City - Montréal
1998	3.50 (22)	4.63 (19)	+1.13
1999	5.07 (14)	3.90 (20)	-1.17
2000	3.82 (28)	4.31 (32)	+0.49
2001	3.69 (16)	3.88 (25)	+0.19
2002	4.18 (33)	4.07 (28)	-0.11
2003	3.96 (24)	3.59 (32)	-0.37

Note: The numbers in brackets indicate the number of files

Table A.15**Changes in the annual indicator of the average stage reached
from 1998 to 2003 for files in the Manufacturing sector****Optimistic scenario**

Year	Montréal	Québec City	Québec City - Montréal
1998	3.49 (35)	3.69 (16)	+0.20
1999	3.02 (53)	3.96 (25)	+0.94
2000	3.76 (45)	5.15 (20)	+1.39
2001	3.57 (72)	3.61 (31)	+0.04
2002	3.25 (60)	3.51 (43)	+0.26
2003	3.62 (79)	3.97 (34)	+0.35

Note: The numbers in brackets indicate the number of files

Table A.16

**Changes in the annual indicator of average stage reached
from 1998 to 2003 for files in the Business Services sector**

Optimistic scenario

Year	Montréal	Québec City	Québec City - Montréal
1998	3.28 (53)	3.57 (28)	+0.29
1999	3.24 (51)	4.35 (37)	+1.11
2000	3.76 (42)	3.66 (29)	-0.10
2001	3.70 (57)	3.48 (29)	-0.22
2002	3.67 (63)	4.20 (20)	+0.53
2003	3.91 (64)	3.19 (27)	-0.72

Note: The numbers in brackets represent the number of files

Table A.17

**Changes in the annual indicator of the average stage reached
from 1998 to 2003 for files in the Restaurant and Hotel Industry**

Optimistic scenario

Year	Montréal	Québec City	Québec City - Montréal
1998	3.23 (39)	3.22 (23)	-0.01
1999	3.33 (36)	3.31 (26)	-0.02
2000	3.73 (30)	4.14 (35)	+0.41
2001	3.58 (43)	3.25 (24)	-0.33
2002	4.11 (38)	4.22 (37)	+0.11
2003	4.00 (23)	4.67 (18)	+0.67

Note: The numbers in brackets indicate the number of files

Table A.18

**Changes in the annual indicator of the average stage reached
from 1998 to 2003 for files in the Other Services sector**

Optimistic scenario

Year	Montréal	Québec City	Québec City - Montréal
1998	2.21 (14)	3.67 (12)	+1.46
1999	3.00 (15)	3.38 (16)	+0.38
2000	3.70 (10)	3.22 (9)	-0.48
2001	4.70 (10)	3.80 (10)	-0.90
2002	4.00 (11)	4.24 (25)	+0.24

2003	4.10	4.67	+0.57
	(10)	(9)	

Note: The numbers in brackets represent the number of files

Table A.19

**Changes in the annual indicator of the average stage reached
from 1998 to 2003 for files in the Wholesale Trade sector**

Optimistic scenario

Year	Montréal	Québec City	Québec City - Montréal
1998	3.11 (28)	2.92 (12)	-0.19
1999	2.75 (20)	3.83 (12)	+1.08
2000	3.30 (23)	4.57 (7)	+1.27
2001	4.21 (28)	3.00 (19)	-1.21
2002	3.55 (22)	4.12 (17)	+0.57

2003	3.71	3.86	+0.15
	(17)	(14)	

Note: The numbers in brackets represent the number of files

Table A.20

**Changes in the annual indicator of the average stage reached
from 1998 to 2003 for the Retail Trade sector**

Optimistic scenario

Year	Montréal	Québec City	Québec City - Montréal
1998	2.91 (44)	3.50 (20)	+0.59
1999	3.44 (36)	3.38 (29)	-0.06
2000	3.00 (37)	3.80 (25)	+0.80
2001	3.69 (29)	3.75 (24)	+0.06
2002	2.30 (40)	4.10 (29)	+1.80

2003	2.44	3.11	+0.67
	(32)	(27)	

Note: The numbers in brackets represent the number of files

Table A.21

**Changes in the annual indicator of the average stage reached
from 1998 to 2003 for files in the Transportation and Warehousing sector**

Optimistic scenario

Year	Montréal	Québec City	Québec City - Montréal
1998	2.57 (7)	4.50 (8)	+1.93
1999	2.91 (11)	4.00 (7)	+1.09
2000	4.04 (27)	5.07 (14)	+1.03
2001	3.14 (14)	4.07 (14)	+0.93
2002	4.18 (11)	3.87 (23)	-0.31

2003	4.71	3.92	-0.79
	(17)	(13)	

Note: The numbers in brackets indicate the number of files

Table A.22

Indicator of the average stage reached based on the amount of ASSETS of files grouped into two categories around the median

Montréal / 1998 – 2003 / Optimistic scenario

Sector	Small	Large	Large - Small
Construction	3.65 (68)	4.33 (69)	+0.68
Manufacturing	3.10 (172)	3.81 (172)	+0.71
Business services	3.41 (164)	3.80 (165)	+0.39
Restaurant and hotel industry	3.06 (104)	4.21 (105)	+1.15
Other services	3.09 (35)	3.91 (35)	+0.82
Wholesale trade	2.96 (69)	3.96 (69)	+1.00
Retail trade	2.43 (108)	3.45 (109)	+1.02
Transportation and warehousing	3.12 (43)	4.43 (44)	+1.31

Table A.23

**Indicator of the average stage reached based on the amount of LIABILITIES
of
files grouped into two categories around the median**

Montréal / 1998 - 2003 / Optimistic scenario

Sector	Small	Large	Large - Small
Construction	4.07 (68)	3.91 (69)	-0.16
Manufacturing	3.53 (172)	3.38 (172)	-0.15
Business services	3.94 (165)	3.27 (165)	-0.67
Restaurant and hotel industry	3.53 (104)	3.74 (105)	+0.21
Other services	3.63 (35)	3.37 (35)	-0.26
Wholesale trade	3.49 (69)	3.42 (69)	-0.07
Retail trade	2.89 (109)	2.98 (109)	-0.09
Transportation and warehousing	3.74	3.82	+0.08

(43)

(44)

Table A.24

Indicator of the average stage reached based on the amount of ASSETS of files grouped into two categories around the median

Québec City / 1998 – 2003 / Optimistic scenario

Sector	Small	Large	Large - Small
Construction	3.82 (76)	4.34 (77)	+0.52
Manufacturing	3.79 (81)	4.20 (82)	+0.41
Business services	3.36 (83)	4.20 (84)	+0.84
Restaurant and hotel industry	3.89 (81)	3.76 (82)	-0.13
Other services	3.15 (40)	4.56 (41)	+1.41
Wholesale trade	3.20 (40)	4.05 (41)	+0.85
Retail trade	3.47 (75)	3.81 (75)	+0.34
Transportation and warehousing	4.18 (38)	4.38 (39)	+0.20

Table A.25

**Indicator of the average stage reached based on the amount of LIABILITIES
of
files grouped into two categories around the median
Québec City / 1998 – 2003 / Optimistic scenario**

Sector	Small	Large	Large - Small
Construction	3.87 (77)	4.23 (77)	+0.36
Manufacturing	3.84 (83)	4.07 (83)	+0.23
Business services	3.56 (84)	3.93 (85)	+0.37
Restaurant and hotel industry	4.10 (81)	3.55 (82)	-0.55
Other services	3.35 (40)	4.37 (41)	+1.02
Wholesale trade	3.25 (40)	4.00 (41)	+0.75
Retail trade	3.45 (76)	3.80 (76)	+0.35
Transportation and warehousing	4.31	4.18	-0.13

(39)

(39)

Table A.26
Indicator of the average stage reached
based on the length of the procedure
Montréal / 1998 – 2003 / Optimistic scenario

Sector	A 820 days or less	B 1185 days or less	B - A
Construction	4.53 (17)	4.03 (40)	-0.50
Manufacturing	3.75 (80)	3.48 (136)	-0.27
Business services	3.94 (72)	3.62 (112)	-0.32
Restaurant and hotel industry	3.65 (52)	3.26 (86)	-0.39
Other services	3.60 (15)	3.31 (26)	-0.29
Wholesale trade	3.81 (42)	3.54 (63)	-0.27
Retail trade	3.32 (57)	2.90 (86)	-0.42
Transportation and warehousing	4.18	3.68	-0.50

(17)

(25)

Table A.27

**Indicator of the average stage reached
based on the length of the procedure**

Québec City / 1998 – 2003 / Optimistic scenario

Sector	A 820 days or less	B 1185 days or less	B - A
Construction	4.28 (67)	4.15 (86)	-0.13
Manufacturing	4.30 (79)	4.07 (95)	-0.23
Business services	3.93 (68)	3.95 (104)	+0.02
Restaurant and hotel industry	3.70 (83)	3.60 (95)	-0.10
Other services	4.16 (31)	3.31 (26)	-0.85
Wholesale trade	4.15 (27)	3.70 (43)	-0.45
Retail trade	3.60 (67)	3.43 (89)	-0.17

Transportation and warehousing

4.07
(30)

4.37
(41)

+0.30