

# What Does “Good Faith” Mean in Insolvency Proceedings?

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## 1. INTRODUCTION

Commercial insolvencies do not have to be, in every instance, a zero sum game — a situation where one party’s gain is equal to another party’s loss. The perception that they are, however, can lead creditors to seek to maximize their own economic gain by minimizing the financial recovery of other stakeholders. Paradoxically, if each creditor precipitously pursues its own economic self-interest, the inevitable result will be the destruction of the very value that creditors are seeking to capture. Well-crafted insolvency regimes anticipate that commercial desperation may lead to aggressive creditor behaviour and the disregarding of the interests of competing stakeholders. The comprehensive stay of proceedings has emerged as the most obvious and blunt judicial and statutory instrument to protect creditors from themselves and each other.

As a result of the stay, a system is imposed on creditors that impairs their legal entitlements. This impairment is not without benefit. The system provides creditors with greater transparency and stability and a forum to seek recourse should they believe the process is not treating them fairly. Informed commentators, however, are questioning whether the scales have been correctly balanced and whether the actions of self-serving creditors are being properly corralled by the existing judicial and statutory infrastructure. There is an ongoing debate as to whether creditors in an insolvency proceeding, made desperate by circumstance, should be subject to an express statutory duty of good faith.<sup>1</sup> A recent decision of the Supreme Court of Canada has fuelled this debate.

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<sup>1</sup> See, e.g., Dr. Janis Sarra, “Examining the Insolvency Toolkit: Report of the Public Meetings of the Canadian Commercial Insolvency Law System” (July 2012), online: < [http://www.insolvency.ca/en/iicresources/resources/Examining\\_the\\_Insolvency\\_Toolkit\\_Dr\\_J\\_Sarra\\_2012.pdf](http://www.insolvency.ca/en/iicresources/resources/Examining_the_Insolvency_Toolkit_Dr_J_Sarra_2012.pdf) > at 12; and “Report of the statutory review of the *Bankruptcy and Insolvency Act* and *Companies’ Creditors Arrangement Act* by the

In November 2014, the Supreme Court of Canada (Supreme Court) released its seminal decision in *Bhasin v. Hyrnew*,<sup>2</sup> and found that there was a common law duty, which applies to all contracts, to act honestly in the performance of contractual obligations. The Supreme Court held that good faith contractual performance is a general organizing principle at common law and is the animating principle behind the sentiment that parties have a duty to act “honestly and reasonably and not capriciously or arbitrarily”<sup>3</sup> and that parties must have “appropriate regard to the legitimate contractual interests of the contracting partner.”<sup>4</sup>

The Supreme Court anticipated the criticism that injecting a principle as malleable and inherently subjective as good faith into commercial dealings would lead to legal uncertainty and frustrate market efficiency. In that regard, the Supreme Court held that parties are free to act in their own economic self-interest, but cannot lie or deliberately mislead a contracting party in furtherance of that self-interest. Indeed, the Supreme Court was of the view that imposing this baseline duty reinforced the legitimate commercial expectations of contractual parties, rather than undermining them.

Accordingly, the findings in *Bhasin* should not be overstated. *Bhasin* calls for a highly contextual and case-specific understanding of what is required to give appropriate consideration to the legitimate interests of both contracting parties; good faith does not require acting to serve the other party’s interests in all cases.<sup>5</sup> A counter-party to a contract is not, by its very nature, a fiduciary, and does not owe a duty of loyalty to another party to the contract. The doctrine articulated by the Supreme Court “merely requires that a party not seek to undermine [a co-contracting party’s] interests in bad faith.”<sup>6</sup> Despite the measured tones of the Supreme Court in evolving the common law in this area, it is clear that the decision will have a broader impact than the law of contract, including in the insolvency field.

In a recent article, Dr. Janis Sarra asserts that the Supreme Court’s reasoning in *Bhasin* has a “direct application” to insolvency cases.<sup>7</sup> Dr. Sarra argues, with typical clarity and eloquence, that express statutory provisions

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legislative review task force (Commercial) of the Insolvency Institute of Canada and the Canadian Association of Insolvency Restructuring Professionals” (15 July 2014) online: < [http://www.insolvency.ca/en/resources/DOCS-13606783-v1-JOINT\\_TASK\\_FORCE\\_REPORT\\_-\\_JULY\\_15\\_2014.PDF](http://www.insolvency.ca/en/resources/DOCS-13606783-v1-JOINT_TASK_FORCE_REPORT_-_JULY_15_2014.PDF) > at p. 11.

<sup>2</sup> 2014 SCC 71, 2014 CarswellAlta 2046, 2014 Carswell Alta 2047 [*Bhasin*].

<sup>3</sup> *Ibid.* at para. 63.

<sup>4</sup> *Ibid.* at para. 65.

<sup>5</sup> *Ibid.*

<sup>6</sup> *Ibid.* at para. 65.

<sup>7</sup> Janis P. Sarra, “La bonne foi est un considération de base — Requiring Nothing Less than Good Faith in Insolvency Law Proceedings” in Janis P. Sarra & Justice Barbara

requiring good faith should be incorporated into our insolvency legislation. Further, such express statutory provisions would be consistent with already existing case law, including *Bhasin*.<sup>8</sup> Dr. Sarra submits that in addition to the requirements set forth in *Bhasin*, “[c]reditors’ conduct should be explicitly required to be in good faith if they expect the full benefit of remedies under insolvency law and contract law to which they may be entitled.”<sup>9</sup>

Notably, the *Companies’ Creditors Arrangement Act* (CCAA) and the *Bankruptcy and Insolvency Act* (BIA) already contain statutorily codified obligations for the principal parties in insolvency proceedings to act in good faith. For example, debtor companies have an affirmative duty to act in good faith to obtain a comprehensive stay of proceedings in an initial order under the CCAA or any extension of the stay. Under the BIA, debtors who file a notice of intention (NOI) to file a proposal receive the benefit of an automatic stay of proceedings, but must act in good faith to extend the stay. In addition, receivers and court-appointed monitors have an affirmative duty to act in good faith, while receivers, monitors, and trustees may only be insulated from liability to the extent that they carry out their duties in good faith.<sup>10</sup>

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Romaine, eds., *Annual Review of Insolvency Law 2014* (Toronto: Carswell, 2014) 145 at 157.

<sup>8</sup> See *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60 at para. 70, (*sub nom. Ted Leroy Trucking Ltd., Re*) 2010 CarswellBC 3419 [*Century Services*]. Dr. Sarra also notes that the Quebec Civil Code already contains requirements to act in good faith and such requirements have already been considered in the insolvency context. See *Banque de Montréal c. TMI Education.com inc. (Faillite)*, 2014 QCCA 1431 (C.A.).

<sup>9</sup> *Supra* note 7 at 149.

<sup>10</sup> The CCAA and BIA also refer to good faith obligations in the following sections, although there is little relevant discussion of good faith in case law applying these provisions:

(a) section 33(3)(b) of the CCAA provides that a debtor may only obtain an order authorizing the debtor to serve a notice to bargain in respect of a collective bargaining agreement (CBA) if the debtor has made “good faith” efforts to renegotiate the provisions of the CBA;

(b) section 36(4)(a) of the CCAA provides that a debtor may sell assets to a related party outside the ordinary course of business only if all of the factors in section 36(3) are met *and* “good faith efforts” were made to sell or otherwise dispose of assets to unrelated parties;

(c) section 50(12)(a) of the BIA provides that a court may, on application by the trustee, an interim receiver or a creditor, declare that a proposal is deemed to have been refused by creditors if the debtor has not acted or is not acting in “good faith and with due diligence”;

(d) section 65.12(2)(b) of the BIA provides that a debtor who has filed a NOI may only obtain an order authorizing the debtor to serve a notice to bargain in respect of

This paper does not seek to resolve fully the debate as to whether the obligation to act in good faith should be expanded to all stakeholders in an insolvency proceeding. It does, however, attempt to assist in informing the debate by reviewing the key cases in which Canadian courts have considered the doctrine of good faith. Canadian courts have had several opportunities to discuss the doctrine as it relates to (i) debtor companies; (ii) court-appointed monitors; (iii) trustees; and (iv) receivers. Given the attention that this issue has received, it is likely that these participants in the insolvency process will have their actions scrutinized more closely, through the crucible of a “good faith” analysis. Thus, precedent will provide guidance as to what conduct will be impugned and what conduct should survive scrutiny. Moreover, in deciding whether to expand the good faith obligation to other stakeholders such as creditors, it is instructive to understand the factual contexts in which the doctrine has already been considered. Following this review, the paper concludes that a further codification or other explicit requirements on creditors or other stakeholders to act in good faith in insolvency proceedings may not be required, given the supervision of the court and the current statutory provisions requiring debtors and court officers to act in good faith.

## 2. THE DEBTOR COMPANY

Both the CCAA and the BIA (proposal provisions) impose duties on the debtor company to act in good faith. The CCAA requires a debtor to demonstrate that it is acting “in good faith and with due diligence” to obtain protection and a stay of proceedings on an initial application.<sup>11</sup> In addition, the debtor needs to satisfy the court that it is continuing to act in good faith in order to obtain an extension to the stay of proceedings.<sup>12</sup>

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the CBA if the debtor has made “good faith” efforts to renegotiate the provisions of the CBA; and

(e) section 65.13(5)(a) of the BIA provides that a debtor who has filed a NOI may sell assets to a related party outside the ordinary course of business only if all of the factors in section 65.13(4) are met *and* “good faith efforts” were made to sell or otherwise dispose of assets to unrelated parties.

<sup>11</sup> See *Century Services*, *supra* note 8 at para. 69, and *Alberta Treasury Branches v. Tallgrass Energy Corp.*, 2013 ABQB 432 at para. 13, 2013 CarswellAlta 1496 [*Tallgrass Energy*]. Although case law has developed a requirement that a debtor act in good faith to obtain an initial order, the provisions of the CCAA only explicitly require that the debtor act in good faith and with due diligence to obtain an extension of the stay. See *Companies’ Creditors Arrangement Act*, R.S.C. 1985, c. C-36, s. 11.02(3).

<sup>12</sup> CCAA, *ibid.*

**a) Obtaining an Initial CCAA Stay of Proceedings**

Canadian courts generally grant an initial 30-day stay without an in-depth analysis of good faith, saving a determination of good faith for when the debtor seeks an extension of the initial stay. However, courts have, on occasion, decided the good faith issue at this stage — typically where there are competing CCAA and receivership applications.

*i) Alberta Treasury Branches v. Tallgrass Energy*

In the 2013 decision of *Alberta Treasury Branches v. Tallgrass Energy Corp.*, the Alberta Court of Queen’s Bench confirmed that “a section 11 [stay] order under the CCAA is not granted merely by the fact of its application.”<sup>13</sup> In other words, unlike under the United States *Bankruptcy Code*, the debtor does not obtain an automatic stay of proceedings simply by filing for CCAA protection. In *Tallgrass Energy*, the Court was met with two applications: one from the company for an initial stay order under the CCAA; and one from secured creditors seeking the appointment of a receiver. In dismissing the CCAA application and granting the receivership order, the Court explained that the CCAA “requires that the court hearing the application exercise its discretion” in determining whether the company has “acted and is acting in good faith and with due diligence.”<sup>14</sup> The Court held that the debtor’s application did not pass this threshold because the debtor’s refinancing options contained no firm commitments and “were not commercially realistic.”<sup>15</sup> Accordingly, the Court decided that this case “would likely be a liquidating CCAA” and that a receivership order was more appropriate.<sup>16</sup> Moreover, the secured lenders had lost faith in the debtor’s management, further militating against a finding of good faith.

*ii) Alexis Paragon Limited Partnership*

More recently, in the 2014 decision of *Re Alexis Paragon Limited Partnership*,<sup>17</sup> the Alberta Court of Queen’s Bench again dealt with competing applications for a CCAA initial order and the appointment of a receiver. While the Court dismissed the CCAA application and appointed a receiver over the debtor’s assets, the Court found that the debtor companies (the Paragon Group) were acting in good faith. The secured creditor took issue with numerous aspects

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<sup>13</sup> *Tallgrass Energy*, *supra* note 11 at para. 13.

<sup>14</sup> *Ibid.*

<sup>15</sup> *Ibid.* at para. 18.

<sup>16</sup> *Ibid.*

<sup>17</sup> 2014 ABQB 65, 2014 CarswellAlta 165 (Q.B.) [*Alexis Paragon*].

of the Paragon Group's conduct, including its "failure to move, in a timely way, to reduce overheads in the Casino operation and to address issues raised by the Alberta Gaming Regulator" as well as "the failure of the Paragon Group to maintain its debt obligations with [the secured creditor] in good standing."<sup>18</sup>

Despite these criticisms, the Court noted that Paragon Group's "principals have continued to inject capital into the operations of the Casino to keep it afloat," which appeared to be "acts of desperation akin to 'Hail Mary' passes, rather than a series of activities demonstrating bad faith."<sup>19</sup> Thus, good faith was not necessarily equated with the debtor's principals making good business decisions, but with the good intentions of trying to save the company, even if the proposed solutions were not viable.

### **b) Extension of Stay Order**

In order to obtain an extension of the initial stay of proceedings, section 11.02(3) of the CCAA requires the applicant to establish: (a) "that circumstances exist that make the [extension] order appropriate" and (b) "that the applicant has acted, and is acting, in good faith and with due diligence."<sup>20</sup>

#### *i) San Francisco Gifts*

The Alberta Court of Queen's Bench's 2005 decision in *Re San Francisco Gifts Ltd.*<sup>21</sup> provides the most comprehensive survey of "good faith" in the context of a request to extend the stay. This case involved an application by the San Francisco group of companies (San Francisco) to extend their stay of proceedings under the CCAA. While a group of landlords opposed the motion on the basis of San Francisco's recent guilty plea under the *Copyright Act* for selling knockoff and illegal goods, the Court found that San Francisco had already been punished for its illegal conduct. Since San Francisco subsequently acted in good faith in working towards a plan of arrangement for its creditors, the Court granted the extension.

After noting that "the term 'good faith' is not defined in the CCAA" and that "there is a paucity of judicial consideration about its meaning in the context of stay extension applications," the Court explained that, regardless of how good faith is defined, honesty and commercial fairness are its key elements.<sup>22</sup> In addition, a debtor's good faith obligation is owed to the court and the stakeholders directly affected by the process, including investors, creditors, and

<sup>18</sup> *Ibid.* at para. 37.

<sup>19</sup> *Ibid.* at para. 38.

<sup>20</sup> CCAA, *supra* note 11, s. 11.02(3).

<sup>21</sup> 2005 ABQB 91, 2005 CarswellAlta 174 (Q.B.) [*San Francisco Gifts*].

<sup>22</sup> *Ibid.* at paras. 14, 16.

employees, although the Court stopped short of requiring a debtor company to act in good faith in its dealings with the public at large.<sup>23</sup>

After reviewing a variety of cases dealing with good faith, the Court ultimately concluded that allowing the stay to continue would not minimize or excuse San Francisco's "repugnant" conduct.<sup>24</sup> Moreover, the effect terminating the stay would have on unsecured creditors — who would be denied their right to vote on a plan and whatever chance they would have for a recovery — was of greater concern to the Court, which justified extending the stay.<sup>25</sup>

*ii) Muscletech Research & Development*

In the 2006 decision of *Re Muscletech Research & Development Inc.*,<sup>26</sup> the Ontario Superior Court of Justice confirmed the time period during which a court should assess a party's conduct for evidence of good faith. This was a motion to extend the stay of proceedings. One party brought forth allegations of bad faith regarding the "past activities" of the debtors, prior to the commencement of the CCAA proceedings. The Court stated, "the question of good faith is with respect to how these parties are conducting themselves in *these CCAA proceedings*."<sup>27</sup> After disregarding the allegations of bad faith, the Court held that the debtors had demonstrated their good faith and due diligence by proceeding according to a clear timetable<sup>28</sup> and the stay of proceedings was extended for an additional month.

*iii) Dura Automotive*

In the 2010 decision of *Re Dura Automotive Systems (Canada) Ltd.*,<sup>29</sup> the Ontario Superior Court of Justice declined to extend the stay of proceedings under the CCAA where the debtor was unable to demonstrate that it was acting in good faith and with due diligence. The main issue in the proceedings was whether the Canadian debtor bore sole liability to pay into a Canadian pension plan or whether this liability was shared by its related entities. While the debtor had negotiated extensively with the unions and pension plan administrator, once it became apparent that these negotiations would not be successful and a viable

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<sup>23</sup> *Ibid.* at para. 17.

<sup>24</sup> *Ibid.* at para. 31.

<sup>25</sup> *Ibid.*

<sup>26</sup> 2006 CarswellOnt 720, [2006] O.J. No. 462, 19 C.B.R. (5th) 57 (S.C.J. [Commercial List]).

<sup>27</sup> *Ibid.* at para. 4 [emphasis added].

<sup>28</sup> *Ibid.*

<sup>29</sup> 2010 ONSC 1102, 2010 CarswellOnt 894 (S.C.J. [Commercial List]).

plan could not be put forward, the debtor quickly reversed its position and sought an order that the plan be presented to the retirees for a vote.

The Court was clear that this “last-minute shift in tactics” led to the “inescapable conclusion that [the debtor] did not act in good faith” in negotiating with the unions and the pension plan administrator and, further, that the debtor “did not act with due diligence by failing to address these representative issues on a timely basis.”<sup>30</sup> As a result, the Court held that the applicant had not met the test under section 11.02(3) of the CCAA, refused to extend the stay of proceedings and permitted creditors to bring bankruptcy applications against the debtor company.<sup>31</sup>

*iv) Envision Engineering & Contracting*

The Ontario Superior Court of Justice’s 2011 decision in *Re Envision Engineering & Contracting Inc.*<sup>32</sup> denied a secured creditor’s motion to extend the initial stay under the CCAA because the debtor had not acted in good faith. After obtaining an initial order, the monitor experienced difficulty in obtaining information regarding the debtor group’s financial affairs.<sup>33</sup> These difficulties were outlined in the monitor’s report which stated that management was no longer “committed to the process and they have not been responsive to the Monitor’s request for information. . .”.<sup>34</sup> While it was a secured creditor who brought the motion, the Court held — despite the language of section 11.02(3)(b) of the CCAA requiring “the applicant” to act in good faith — that the debtor’s lack of good faith and due diligence was fatal to the relief sought by the secured creditor.<sup>35</sup>

**c) Extension of Time to File a Proposal**

The test to obtain a stay extension in an NOI proceeding under the BIA is more onerous than the test to obtain a stay extension under the CCAA. Section 50.4(9) of the BIA provides that, in order to obtain a stay extension, the debtor must prove to the court on a balance of probabilities that: (i) the debtor has acted in good faith and with due diligence; (ii) the debtor will likely be able to make a viable proposal; and (iii) no creditor will be materially prejudiced by the extension.<sup>36</sup>

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<sup>30</sup> *Ibid.* at para. 38.

<sup>31</sup> *Ibid.* at paras. 41, 43.

<sup>32</sup> 2011 ONSC 631, 2011 CarswellOnt 371 (S.C.J.).

<sup>33</sup> *Ibid.* at para. 7.

<sup>34</sup> *Ibid.* at para. 12.

<sup>35</sup> *Ibid.* at para. 21.

<sup>36</sup> *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 50.4(9).



Conversely, section 50.4(11) of the BIA provides that creditors may seek to terminate the stay if they can establish that: (i) the debtor is not acting in good faith or with due diligence; (ii) the debtor will likely not be able to file a viable proposal or a proposal that would be accepted by the creditors prior to the expiration of the stay period; or (iii) the creditors as a whole would be materially prejudiced by the continuation of the stay.<sup>37</sup>

*i) H&H Fisheries*

In the 2005 decision of *Re H&H Fisheries Ltd.*,<sup>38</sup> the Supreme Court of Nova Scotia granted an extension of time for the debtor to file a proposal, emphasizing that the onus was on the debtor to satisfy the court on a balance of probabilities that each of the prerequisites of section 50.4(9) had been established.<sup>39</sup>

The good faith issue arose in light of the fact that the debtor had signed a commitment letter with the Bank of Nova Scotia (BNS) agreeing to have all of its operating accounts at that bank. Subsequent to signing the commitment letter but before filing the NOI, the debtor began to experience cash flow problems and started to deposit funds with the Canadian Imperial Bank of Commerce (CIBC), in order to avoid the funds being applied in satisfaction of the obligations owing to its creditor, BNS. In considering the requirements of section 50.4(9) of the BIA, the Court determined that breach of a contract does “not necessarily” constitute bad faith.<sup>40</sup> In follow-up discussion, the Court fleshed out the distinction between good faith and bad faith actions:

The converse of good faith is bad faith and bad faith requires a *motivation and conduct that is unacceptable*. If, for example, the diversion of operating/trading proceeds had been diverted to the CIBC for the purposes of personal gain for any officer, director or shareholder of [the debtor]. . . then clearly such would amount to bad faith and quite possibly fraud. *It is clear that the motivation for moving funds to the CIBC account was, in one word, for the purpose of “survival”*. Funds were essential in that I accept the view expressed by [the debtor] that had it continued to direct its operating/trading funds to BNS the probability is almost a certainty that BNS would have utilized such funds to pay-down its advances precluding the [debtor] company from having any operating funds and the door to the [debtor’s fish processing] plant would have been shut.<sup>41</sup>

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<sup>37</sup> *Ibid.* at s. 50.4(11).

<sup>38</sup> 2005 NSSC 346, 2005 CarswellNS 541 (S.C.) [*H&H Fisheries*].

<sup>39</sup> *Ibid.* at para. 12.

<sup>40</sup> *Ibid.* at para. 16.

<sup>41</sup> *Ibid.* at para. 17 [emphasis added].

The Court also made it clear that fraud is not a requirement for a party to fall short of good faith. In this case, the Court found that the debtor breached several other elements of the commitment letter but that the debtor responded by providing documentation, bank records, reconciliation of invoices, and cash withdrawals.

The *H&H Fisheries* Court asserted that acting in good faith could be determined through the absence of bad faith. Moreover, the *H&H Fisheries* Court held that it is critical for courts to assess the base motivation for any impugned conduct and that the legitimate intention to help a company survive is indicative of acting in good faith.

ii) *Entegrity*

In the two 2009 decisions of *Re Entegrity Wind Systems Inc.*,<sup>42</sup> the Prince Edward Island Supreme Court granted a first stay extension under section 50.4(9) of the BIA, but then refused to grant a second stay extension on the basis that the debtor had not acted in good faith and with due diligence.

In the first motion, the company's largest creditor argued that because the debtor had diverted funds that were owing to it pursuant to its credit agreement in order to pay bills and make payroll payments, the debtor was acting in bad faith.<sup>43</sup> After reviewing the debtor's evidence, the Court explained that it was "not of the view [that the debtor] failed to act in good faith during this tumultuous period," but rather, "it appears [that the debtor] was attempting to address [its primary creditor's] demands and in the course of doing so, used funds from projects as well as its own funds *to maintain the company while it moved on an overall plan to extricate itself from its difficulties.*"<sup>44</sup> Much like in *H&H Fisheries*, the Court was willing to look at the underlying motivations for the debtor's actions (trying to save the company) in order to find a good faith explanation for the debtor's actions.

In the second motion, the Court found that in the intervening period, the debtor engaged in unnecessary rent disputes and delayed meeting with Prince Edward Business Development Inc. to seek necessary funding for a proposal. This "inaction" on the debtor's primary goal of developing a viable proposal demonstrated that the debtor had not made sufficient progress to pass the "good faith and due diligence" threshold.<sup>45</sup> Thus, the further stay extension was not granted.

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<sup>42</sup> 2009 PESC 25, 2009 CarswellPEI 47 (S.C.) [*Entegrity 1*]; *Entegrity Wind Systems Inc., Re*, 2009 PESC 33, 2009 CarswellPEI 63 (S.C.) [*Entegrity 2*].

<sup>43</sup> *Entegrity 1*, *ibid.* at para. 7.

<sup>44</sup> *Entegrity 2*, *supra* note 42 at para. 10 [emphasis added].

<sup>45</sup> *Ibid.* at paras. 6–19.

iii) *Com/Mit Hitech Services*

In *Re Com/Mit Hitech Services Inc.*,<sup>46</sup> the Court was faced with an application by a secured creditor under section 50.4(11) of the BIA to terminate the 30-day period for a debtor to file a proposal. Just prior to the debtor filing the NOI, the secured creditor had entered into a new credit arrangement requiring that the “debt equity levels be restored to 3:1 by way of cash infusion/repatriation. . .”<sup>47</sup> However, the debtor made additional investments in the acquisition of the assets of another business in clear contravention of the credit arrangement. The Court considered these actions (which took place prior to the filing of the NOI) and concluded that because the debtor had gone “essentially in a 180 [degree] way against” what it had agreed to with the secured creditor, the debtor had not acted in good faith and with due diligence. As a result, the secured creditor’s motion was granted and the 30-day period to file a proposal was terminated.

d) **Approval of a Proposal**

Once a BIA proposal is accepted by the requisite majority of creditors,<sup>48</sup> Canadian courts have developed a three-pronged test that must be satisfied before the court will sanction the proposal: it must be (i) reasonable; (ii) calculated to benefit the general body of creditors; and (iii) made in good faith. While the first two factors are explicitly contained in section 59(2) of the BIA, courts have implied the good faith requirement as an exercise of their equitable jurisdiction.<sup>49</sup> Generally, in the context of approving a proposal, good faith is equated with full disclosure by the insolvent person.

i) *Kitchener Frame*

In *Re Kitchener Frame Ltd.*, the Ontario Superior Court of Justice heard an unopposed motion to sanction a proposal. In its discussion of the requirements under section 59(2), the Court explained that “[w]ith respect to the requirement of the proposal being made in good faith, *the debtor must satisfy the court that it has provided full disclosure to its creditors of its assets and encumbrances against such assets.*”<sup>50</sup> The Court held that the debtors fulfilled this requirement by

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<sup>46</sup> 1997 CarswellOnt 2753, [1997] O.J. No. 3360 (Bkcty.).

<sup>47</sup> *Ibid.* at para. 2.

<sup>48</sup> A numerical majority of creditors, representing two-thirds in value of the voting claims in each class of creditors.

<sup>49</sup> *Kitchener Frame Ltd., Re*, 2012 ONSC 234, 2012 CarswellOnt 1347 (S.C.J. [Commercial List]) [*Kitchener Frame*]; *Mayer, Re*, 1994 CarswellOnt 268 at para. 6, 25 C.B.R. (3d) 113 (Bkcty.) [*Mayer*].

involving creditors through negotiations with the union and non-union representative counsel, as well as by “widely disseminat[ing] information regarding their BIA proposal proceedings through the media and through postings on the Proposal Trustee’s website.”<sup>51</sup> As a result of the full and adequate disclosure provided by the applicants throughout the proceeding, the Court concluded that the applicants had acted in good faith and sanctioned the proposal.

ii) *Mayer*

In *Re Mayer*, the proposal required creditors to accept the debtor’s equity in the premises in which the debtor resided (Premises) in full satisfaction of the creditors’ claims. The Court noted that an insolvent person asking for the court’s approval of a proposal must do so in good faith, which requires “full disclosure.”<sup>52</sup> However, it was not disclosed anywhere in the proposal (or in the proposal trustee’s report to the court) that: (i) the Premises were held jointly with the insolvent person’s spouse; (ii) the Premises were encumbered by two mortgages; and (iii) \$24,000 in municipal tax arrears were outstanding.<sup>53</sup> As a result of this lack of disclosure, the Court found that the debtor had not acted in good faith and rejected the proposal.

### 3. THE COURT-APPOINTED MONITOR

The monitor, who must be a licensed trustee in bankruptcy, is an officer of the court. The monitor plays a supervisory and an advisory role in CCAA proceedings. In its supervisory role, the monitor oversees the actions of the debtor company while under CCAA protection, on behalf of all creditors and other stakeholders, including employees, customers, and suppliers. In its advisory role, the monitor assists the debtor company’s management in dealing with the restructuring and other issues that arise. The monitor must not be an advocate for the debtor, a particular creditor, or any other stakeholder in the CCAA process.<sup>54</sup> Its duty is to impartially evaluate the activities of the debtor company and make an independent analysis of the debtor’s actions in reports to the court and creditors.<sup>55</sup>

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<sup>50</sup> *Kitchener Frame, ibid.* at para. 35 [emphasis added].

<sup>51</sup> *Ibid.*

<sup>52</sup> *Mayer, supra* note 48 at para. 6.

<sup>53</sup> *Ibid.* at para. 8.

<sup>54</sup> See Kevin P. McElcheran, *Commercial Insolvency Law in Canada*, 2d ed. (Markham, Ont.: LexisNexis, 2011) at 245.

<sup>55</sup> *Ibid.*

The CCAA provides a broad affirmative duty of good faith for court-appointed monitors. Section 25 of the CCAA provides that “[i]n exercising any of his or her powers or in performing any of his or her duties and functions, *the monitor must act honestly and in good faith. . .*”<sup>56</sup> Moreover, monitors must act in good faith to be insulated from liability for their activities undertaken as monitor. Section 23(2) of the CCAA states that “[i]f the monitor acts in good faith and takes reasonable care” in preparing the numerous reports it is obligated to file with the court “the monitor is not liable for loss or damage to any person resulting from that person’s reliance on the report.”<sup>57</sup> While there is a dearth of case law dealing with these provisions or explaining what constitutes a monitor acting in good faith, the Alberta Court of Queen’s Bench decision in *Re Winalta Inc.*<sup>58</sup> provides the clearest and most direct analysis of a monitor’s duties under the CCAA.

**a) Winalta**

In *Winalta*, the Court considered a monitor’s fee application that was opposed by the debtor companies. The debtor companies took issue with the monitor’s bill for various reasons, including that the monitor overcharged, was not transparent in its dealings, and breached its fiduciary duty to all stakeholders.

The debtor companies had obtained an initial order specifically authorizing the monitor to provide the major secured creditor with any financial reports generated by the debtors, which was a condition of the secured creditor’s support for the CCAA proceedings. The debtors prepared regular cash flow statements that were provided to the secured creditor. In addition, the monitor used information contained in the debtors’ regular cash flow statements to generate Net Realization Value Reports (NRVR) for the sole benefit of the secured creditor. The purpose of the NRVR was to enable the secured creditor to determine whether to continue to support the CCAA proceedings or to seek the appointment of a receiver.

The September 2010 NRVR was critical. At that time, the debtors had arranged conditional financing to take out the secured creditor, but they required additional funding from the secured creditor to defray takeout financing costs. However, the September NRVR caused the secured creditor to refuse providing such funding and the debtors had to scramble to find the additional funding from an alternate source. The debtors asserted that the

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<sup>56</sup> *CCAA*, note 11, s. 25(3) [emphasis added].

<sup>57</sup> *Ibid.* at s. 23(2).

<sup>58</sup> 2011 ABQB 399, 2011 CarswellAlta 2237 (Q.B.).

monitor breached its fiduciary duty by delivering the September NRVR to the secured creditor without the debtors' knowledge or consent.<sup>59</sup>

During its review of a monitor's fiduciary and ethical duties, the Court framed its analysis by outlining the monitor's affirmative duty to act in good faith under section 25 of the CCAA. While these actions appeared to be permissible under the initial order, the Court held that the monitor breached its fiduciary duty to the debtors, asserting that the monitor "exceeded its statutory and court ordered authority" by conducting the analysis in the September NRVR and providing it to the secured creditor.<sup>60</sup> This was contrary to the monitor's duty to "ensure that no creditor has an advantage over another."<sup>61</sup> The Court concluded that the monitor did not conduct itself in an open and transparent manner, and that its actions in preparing the September NRVR and delivering it to the secured creditor put it into conflict with the debtors.<sup>62</sup>

The Court observed that that the monitor "lost sight of the bright line separating its duties as an impartial court officer and a private consultant to [the secured creditor]," thereby creating a perception of bias.<sup>63</sup> As a result, the Court reduced a portion of the monitor's fees related to the September NRVR and required the monitor to provide further fee affidavits, at its own cost.

While the Court does not expressly use the language of "good faith" throughout the decision, the case is instructive on how a court may apply a good faith analysis in its assessment of a monitor's activities.

#### 4. TRUSTEES UNDER THE BIA

When a debtor becomes bankrupt under the BIA, the debtor ceases to have legal capacity to dispose of its assets or otherwise deal with its property (excluding property held in trust), which vests in a trustee in bankruptcy. In a proposal proceeding under the BIA, the proposal trustee assists the debtor in developing a proposal and its negotiations with creditors and other key stakeholders.

The BIA generally provides professionals, including trustees, with protection from liability while acting in their professional capacity, as long as they act in good faith. Specifically:

The BIA offers trustees, receivers and similar insolvency professionals protection from liability for their activities in connection with a proceeding under the [BIA]. The statutory framework requires the assistance of these

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<sup>59</sup> *Ibid.* at paras. 70–72.

<sup>60</sup> *Ibid.* at para. 126.

<sup>61</sup> *Ibid.* at para. 77.

<sup>62</sup> *Ibid.* at para. 112.

<sup>63</sup> *Ibid.* at para. 113.

professionals, who would likely be unwilling to serve absent protection for their good faith and duly diligent activities. . .<sup>64</sup>

For example, section 171(6)<sup>65</sup> of the BIA provides that a trustee is not liable for any statements made or opinions expressed in good faith in relation to the report the trustee is required to file with the Superintendent of Bankruptcy. In addition, in the two situations where proposal trustees are required to file cash-flow statements and reports thereon with the Court, sections 50(9) and 50.4(5) of the BIA provide that “[i]f the trustee acts in good faith and takes reasonable care in reviewing the cash-flow statement, the trustee is not liable for loss or damage to any person resulting from that person’s reliance on the cash-flow statement.”<sup>66</sup>

While trustees do not have an affirmative duty to act in good faith under the BIA, as monitors do under section 25 of the CCAA, courts generally consider whether a trustee has acted in good faith when determining whether or not to uphold the trustee’s actions.

#### a) **Katz**

The Ontario Court of Justice’s 1991 decision in *Re Katz*<sup>67</sup> dealt with a motion by the bankrupt to set aside the trustee’s sale of a lawsuit initiated by the bankrupt to a defendant in that action. The former *Bankruptcy Act* provided that the trustee may sell assets with permission of the inspectors<sup>68</sup> and for such consideration as the inspectors may approve. While the sole inspector approved the sale, the Court explained that “the trustee must still exercise appropriate skill and demonstrate good faith.”<sup>69</sup> In these circumstances, the Court held that it was a legitimate business decision for the trustee to resolve the litigation “which may or may not have merit and which may, if meritorious, expose the defendant to financial risk of some degree but will involve some unrecoverable expense in the litigation process, some imposition on the time of the witness and the uncertainties of litigation.”<sup>70</sup> Thus, the trustee sold the litigation in accordance with its business judgment, which was sufficient to establish that the trustee acted in good faith.<sup>71</sup>

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<sup>64</sup> Lloyd W. Houlden, Geoffrey B. Morawetz & Janis P. Sarra, “The 2014-2015 Annotated Bankruptcy and Insolvency Act” (Toronto: Carswell, 2015), at C§16.

<sup>65</sup> BIA, *supra* note 36, s. 171(6).

<sup>66</sup> BIA, *ibid.* at ss. 50(9), 50.04(5).

<sup>67</sup> 1991 CarswellOnt 192, [1991] O.J. No. 1369 (Bkcty.) [*Katz*].

<sup>68</sup> Inspectors are creditor representatives, appointed in certain cases, who must approve certain actions undertaken by the trustee.

<sup>69</sup> *Supra* note 67 at para. 4.

<sup>70</sup> *Ibid.*

**b) Graham Mining (Part 1)**

In *Re Graham Mining Ltd.*,<sup>72</sup> the trustee and receiver (who were one and the same) brought a motion for approval of a proposed settlement of all lawsuits involving the debtor (the debtor was the plaintiff/defendant by counterclaim in one lawsuit and the defendant in another). Opposing creditors brought a cross-motion to reverse the receiver/trustee's decision to accept the proposed settlement of the outstanding litigation.

The Court noted that, in general, trustees in bankruptcy may, with the permission of the inspectors, compromise and settle any debts owing to the bankrupt and any claim made by or against the estate. Moreover, courts will not interfere with a trustee's exercise of its discretion as long as the trustee "acted in good faith and the decision is not unreasonable in the circumstances and is for the benefit of the estate."<sup>73</sup> A court will only hold that a trustee has made a decision in bad faith where "there is a lack of *bona fides* or it is unreasonable from the standpoint of the estate."<sup>74</sup>

In *Graham Mining*, the litigation involving the debtor that was settled was "not easily marketable. . . particularly where its value is uncertain and is subject to set-off and where the costs of realization are unpredictable and could be substantial and exceed the recovery."<sup>75</sup> In light of the many factors at play in valuing this proposed settlement, the Court was "satisfied that the trustee had acted honestly and in good faith and in a commercially reasonable manner in the circumstances" by accepting the proposed settlement of all of the litigation.<sup>76</sup> The trustee's reasonable business judgment was granted a significant level of deference from the supervising court.

**c) Braich**

In the 2003 decision *Re Braich*,<sup>77</sup> the British Columbia Supreme Court approved a trustee's settlement of a debt and dismissed the application by a creditor for an order under section 38 of the BIA<sup>78</sup> to enable the creditor to take

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<sup>71</sup> *Ibid.* at para. 11.

<sup>72</sup> 2001 CarswellOnt 1857, [2001] O.J. No. 21600 (Bkcty.), affirmed 2002 CarswellOnt 1503 (C.A.) [*Graham Mining*].

<sup>73</sup> *Ibid.* at para. 55.

<sup>74</sup> *Ibid.* at para. 54.

<sup>75</sup> *Ibid.* at para. 51.

<sup>76</sup> *Ibid.* at para. 71.

<sup>77</sup> 2003 BCSC 1789, 2003 CarswellBC 2957 (S.C. [In Chambers]) [*Braich*].

<sup>78</sup> Section 38 of the BIA provides that a creditor of the bankrupt estate can obtain the trustee's right to pursue estate litigation where the trustee refuses or fails to pursue such litigation.



action in his own name and expense to set aside alleged fraudulent preferences. The Court agreed with the trustee's opinion — based on independent legal advice — that the fraudulent preference claims were “risky.”<sup>79</sup> Without a detailed analysis of the factors involved in determining good faith, the Court found that the trustee had “negotiated the settlement in good faith” and that the settlement decreased the risk to the bankrupt estate of recovering nothing on the debt.<sup>80</sup> In response to the creditor's desire to pursue the fraudulent preference action himself, the Court explained that “the risk of losing the fraudulent preference action is not illusory and thus, the settlement action taken by the Trustee was not only in good faith, but appropriate in the circumstances.”<sup>81</sup>

#### d) **Solarc Construction**

In the 2009 decision of the Ontario Superior Court of Justice in *Re Solarc Construction Ltd.*,<sup>82</sup> the trustee successfully opposed a motion by the bankrupt and three judgment creditors (the “Application Creditors”) to approve a negotiated settlement with its creditors, suspecting preferential treatment of certain creditors. The trustee subsequently brought a motion seeking costs jointly and severally on a substantial indemnity basis against a law firm representing the Application Creditors and the law firm representing the bankrupt. The law firms representing the Application Creditors and the bankrupt moved for their costs to be recoverable against the trustee personally.

The Court resolved this matter by dismissing both the trustee's motion and the cross-motion on the basis that both parties had acted in good faith. Even though “it was very improbable that the motion for approval of the proposed settlement would have success,” the Court explained that there was “no evidence of bad faith” (which, like in *Bhasin*, is often sufficient to demonstrate good faith) and that “counsel for the Application Creditors and the Bankrupt were entitled to bring their motion forward and argue their case whatever its probability of success.”<sup>83</sup>

Likewise, the Court found that the trustee acted “conscientiously” and “in good faith to ensure that all creditors were treated fairly and equitably.”<sup>84</sup> As in the case with court-appointed monitors (see *Winalta*, above), trustees act in good faith where they fairly and appropriately consider the interests of all creditors, without preferring a specific subset of creditors or stakeholders.

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<sup>79</sup> *Braich*, *supra* note 77 at para. 11.

<sup>80</sup> *Ibid.* at para. 20.

<sup>81</sup> *Ibid.*

<sup>82</sup> 2009 CarswellOnt 392, 174 A.C.W.S. (3d) 936 (S.C.J.) [*Solarc*].

<sup>83</sup> *Ibid.* at para. 36.

<sup>84</sup> *Ibid.* at para. 33.

## 5. RECEIVERS

A receiver (or receiver and manager)<sup>85</sup> may be appointed privately by a secured creditor pursuant to the terms of a security agreement or by court order. A privately appointed receiver's duties are primarily owed to the appointing creditor, while court-appointed receivers are officers of the court and have duties to all stakeholders of the debtor.

Both privately appointed and court-appointed receivers are subject to section 247 of the BIA,<sup>86</sup> which imposes obligations on a receiver to deal with the property of the insolvent person or bankrupt in a "commercially reasonable manner" and to "act honestly and in good faith." Notably, the broad nature of this affirmative duty of good faith poses concern for some commentators.<sup>87</sup>

### a) *Ostrander v. Niagara Helicopters*

In *Ostrander v. Niagara Helicopters Ltd.*,<sup>88</sup> a receiver was appointed privately by a secured creditor upon default by the debtor under a debenture. The debtor subsequently asked the Court to declare numerous transactions undertaken by the receiver null and void and to appoint a new receiver-manager, basing "all of these claims for relief on his allegations that the [receiver and other defendants] have conspired against him, have wrongfully converted assets and have committed fraud and breaches of trust."<sup>89</sup>

While the Court found all of these claims to be "unfounded and without merit,"<sup>90</sup> the court provided insight into the duties owed by a receiver. The Court explained that a privately appointed receiver owes a "duty to everybody to act in good faith and without fraud," but such a duty does not rise to the level of the fiduciary obligation that is owed by the receiver-manager to the appointing creditor.<sup>91</sup> The receiver's general duty required that it undertake a robust sales process to obtain the best offer possible for the debtor's property, as any surplus would revert to the debtor's estate. The Court held that as long as a privately appointed receiver acts "reasonably in the conduct of the business and

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<sup>85</sup> In general, a receiver is appointed to take possession of and sell or liquidate the assets secured by a security agreement in order to repay the outstanding debt. A receiver-manager typically operates and manages the business until it is sold as a going concern. Both receivers and receiver-managers can be appointed privately or by court order and are subject to the same duties of good faith.

<sup>86</sup> *BIA*, *supra* note 36, s. 247.

<sup>87</sup> See McElcheran, *Commercial Insolvency in Canada*, *supra* note 54 at 205.

<sup>88</sup> 1973 CarswellOnt 325, 1 O.R. (2d) 281, 40 D.L.R. (3d) 161 (H.C.).

<sup>89</sup> *Ibid.* at para. 3.

<sup>90</sup> *Ibid.*

<sup>91</sup> *Ibid.* at para. 6.

of course without any ulterior interest” and as long as the receiver ensures that a fair sale is conducted and that the receiver-manager ultimately makes a proper accounting to the debtor/mortgagor, its duty of good faith will be satisfied.

**b) Graham Mining (Part 2)**

The aforementioned case of *Re Graham Mining Ltd.* also sheds light on the duty of good faith with respect to receivers, since both the trustee and receiver in that case were moving for approval of a proposed settlement of litigation involving the debtor. The Court noted that a privately appointed receiver is the agent of the secured creditor that appointed it and that it owes no fiduciary duty to the debtor.<sup>92</sup> However, in exercising its powers to sell the debtor’s property, the Court reiterated a privately appointed receiver must act honestly and in good faith, and deal with the property in a commercially reasonable manner. In this case, the receiver applied to the Court for directions in relation to its obligation to act honestly and in good faith.

The Court held that even if a settlement is not ideal, a receiver need not take on the risks of uncertain litigation if the receiver believes that the cause of action is not meritorious or that the cost could exceed the recovery.<sup>93</sup> Thus, the Court found that, by settling the litigation, the receiver had not breached any obligation imposed on it in respect of realizing on the debtor’s security.<sup>94</sup> Again, this decision emphasizes that the duty of good faith does not always mandate the best decision (in hindsight) or one that maximizes return. The decision to make a safe settlement without the risks of litigation fulfilled the receiver’s duty of good faith.

**c) Bank of Montreal v. Sportsclick**

In the 2009 decision of *Bank of Montreal v. Sportsclick Inc.*,<sup>95</sup> the Nova Scotia Supreme Court considered an opposed motion to approve an interim receiver’s sale of shares owned by the bankrupt company. The sale was opposed on the basis that a higher price could be obtained if the receiver advertised more broadly. Under the current offer, the sale would barely cover the costs of advertising the shares.<sup>96</sup>

The Court noted that “commercial reasonableness” depends on “the circumstances of the sale, including a consideration of the variables such as the method of sale, the subject matter of the sale, advertising or other methods of

<sup>92</sup> *Graham Mining*, *supra* note 72 at para. 45.

<sup>93</sup> *Ibid.* at paras. 49–50.

<sup>94</sup> *Ibid.* at para. 53.

<sup>95</sup> 2009 NSSC 354, 2009 CarswellNS 649 (S.C.) [*Sportsclick*].

<sup>96</sup> *Ibid.* at para. 21.

exposure to the public, the time and place of the sale, and related expenses.”<sup>97</sup> Moreover, the receiver is under a particular duty to make a sufficient effort to get the best possible price for the assets but it has no duty (of good faith or otherwise) to actually obtain the best possible price.<sup>98</sup>

The Court reaffirmed the position that courts should be deferential when assessing the good faith of a receiver and should generally defer to the receiver’s business judgment at the time the decision is made:

The decisions made by the Receiver were made in good faith, cognizant of the duties that a Receiver is subject to. It made business judgments that may be easy, with the benefit of hindsight, to criticize, but they were reasonable having regard to the circumstances in existence at the time. No alternatives to the targeted marketing approach have been shown to exist that would provide, beyond speculation, a potential for a greater return.<sup>99</sup>

Given that the tendering process “was carried out in a transparent and fair manner, consistent with industry standards,”<sup>100</sup> the Court was convinced that the receiver acted in good faith and could not attribute any bad faith to the receiver. Thus, the *Bank of Montreal v. Sportslick* court examined the requirements of commercial reasonableness in detail, found that the receiver acted in a commercially reasonable manner, and therefore concluded that the receiver acted in good faith.

#### **d) Aquilon Capital v. Sucor**

In *Aquilon Capital Corp. v. Sucor Ltd.*,<sup>101</sup> the New Brunswick Court of Queen’s Bench denied an application for an order that a privately appointed receiver be replaced and for any agreement of purchase and sale of the company’s assets be terminated and held to be of no force and effect. The applicant (Aquilon) was a subordinate secured creditor of the debtor and sought to restrain the sale of certain of the debtor’s assets because Aquilon’s principal had also submitted a bid for the debtor’s assets through his personal investment company. The Court held that unsuccessful bidders for the debtor company’s assets were not owed any duty of good faith by the receiver.<sup>102</sup>

In addition, the Court held that courts should be “extremely reluctant” to set aside a decision of a privately appointed receiver, who owes a fiduciary duty

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<sup>97</sup> *Ibid.* at para. 63.

<sup>98</sup> *Ibid.*

<sup>99</sup> *Ibid.* at para. 65 [emphasis added].

<sup>100</sup> *Ibid.* at para. 66.

<sup>101</sup> 2010 NBQB 144, 2010 CarswellNB 222 (Q.B.).

<sup>102</sup> *Ibid.* at para. 24.

to the creditor that appointed it, but no one else,<sup>103</sup> although a receiver has a lesser duty to act in good faith towards other stakeholders. Here, the Court found that, based on the evidence, the receiver had acted honestly and in good faith because it “did everything within its power to sell the assets of [the debtor]; conducted a sale process which was fair and reasonable and entered into an agreement for the purchase and sale of the Receivership Assets for a price which it considered to be fair.”<sup>104</sup> As in *Bank of Montreal v. Sportsclick*, the Court analyzed some of the same factors that courts consider when determining whether a receiver has acted in a commercially reasonable manner.<sup>105</sup> The Court was persuaded that the receiver had solid grounds for rejecting the applicant’s offer by the fact that the offer was “loaded with conditions”.<sup>106</sup>

Given that there was no evidence that the receiver acted in a commercially unreasonable manner, the Court held that the receiver acted in good faith. The Court appears to have conflated the commercial reasonableness standard and the good faith test such that if a receiver is found to have acted in a commercially reasonable manner, it necessarily acts in good faith.

## 6. CONCLUSION

While the term “good faith” is not defined in the CCAA or the BIA, the cases discussed above indicate that to act in good faith, a debtor must act with basic honesty, commercial fairness, and good intentions towards all stakeholders in the insolvency process.<sup>107</sup> Critically, this analysis looks at the underlying motivation and the conduct of the debtor in determining good faith. Courts have consistently held that actions taken for the purpose of enabling the business to survive are considered to be undertaken in good faith.<sup>108</sup> Moreover, as the Supreme Court held in *Bhasin*, insolvency courts often determine whether a party has acted in good faith on the basis that such party has not acted with motives that constitute bad faith.<sup>109</sup> In addition, courts have implied a good faith requirement on the part of a debtor before a court will approve a proposal to creditors under the BIA. In this instance, good faith refers to the full and frank disclosure required by the insolvent person of its assets, liabilities, and the true terms and conditions of the proposal.

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<sup>103</sup> *Ibid.* at para. 30.

<sup>104</sup> *Ibid.* at para. 31.

<sup>105</sup> See *Sportsclick*, *supra* note 95 at para. 45.

<sup>106</sup> *Aquilon*, *supra* note 101 at paras. 35–36.

<sup>107</sup> *San Francisco Gifts*, *supra* note 21 at paras. 14, 16–17.

<sup>108</sup> See *Alexis Paragon*, *supra* note 17 at para. 38; *H&H Fisheries*, *supra* note 38 at para. 17; *Entegrity*, *supra* note 42 at para. 10.

<sup>109</sup> *H&H Fisheries*, *ibid.* at para. 17.

Monitors appointed under the CCAA have an overarching duty to act in good faith. While there is little case law analyzing the terms of a monitor's duty of good faith, a monitor must act impartially and ensure that it does not act (or appear to act) to prefer one creditor's interests over another.<sup>110</sup> The monitor is also required to operate in an open and transparent manner with respect to the debtor, the creditors and the court.<sup>111</sup>

Trustees under the BIA act in good faith as long as they make legitimate business decisions for the benefit of the estate that are "not unreasonable" in the circumstances.<sup>112</sup> Courts will only find bad faith where a trustee's decision is unreasonable from the estate's point of view. Moreover, trustees must treat all creditors fairly and equitably in a proceeding under the BIA.<sup>113</sup>

Receivers have a two-pronged obligation to "act honestly and in good faith" and to deal with a debtor's property in a "commercially reasonable manner." Courts have generally held that if a receiver deals with property in a commercially reasonable manner, the receiver has satisfied the obligation to act in good faith. In other words, the two-pronged obligation appears to have been conflated into a single test of commercial reasonableness.

Unlike the debtor and court officers, creditors are not subject to an express statutory duty of good faith, but they can hardly operate with impunity. All material transactions, contracts, and other commercial dealings with the debtor company (such as debtor-in-possession credit agreements, plan support agreements, and agreements of purchase and sale) are typically subject to review by a court officer with good faith and fiduciary duties and, more importantly, review and approval by the court. Of course, any attempt to lift the stay to enforce contractual remedies is subject to court approval or court officer consent. That approval or consent would not be granted to further any malevolent intent. Further, *Bhasin* already establishes that lying or deliberately misleading a counter-party in contractual dealings is beyond the pale.

With the existing level of oversight already in place and the evolution of the common law initiated by the Supreme Court, it is not evident why further constraints should be placed on creditors who have been conscripted into participating in the insolvency process.

In the final analysis, the existing judicial and statutory infrastructure provides a protective shell against the bad faith conduct of creditors in an insolvency. While the imposition of the additional duty of good faith seems constructive at first consideration, it may bring with it a significant degree of commercial uncertainty. For example, assume a creditor that is out of the money

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<sup>110</sup> *Winalta*, *supra* note 58 at para. 114.

<sup>111</sup> *Ibid.* at para. 81.

<sup>112</sup> *Katz*, *supra* note 67 at para. 11; *Graham Mining*, *supra* note 72 at para. 55.

<sup>113</sup> *Solarc*, *supra* note 82 at para. 33.

in a liquidation would receive some dividend in a reorganization plan, but, nonetheless wants to vote against the plan, on the theory that it can extract greater value by taking an obstructionist view. Or perhaps the creditor simply wants the plan to fail for some collateral purpose. Is that creditor acting in bad faith? Should its vote be counted? Should the creditor be entitled to vote as it wishes, whatever its commercial motivation? This is one illustration of the uncertainty regarding what good faith requires in the context of creditor action which may ultimately have a paralyzing effect on negotiations, add greater litigation costs, impair efficiency, and alter the carefully calibrated balance between the rights of creditors and their insolvent debtors.<sup>114</sup>

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<sup>114</sup> See McElcheran, *Commercial Insolvency in Canada*, *supra* note 54 at 205, for a discussion of this concern in the context of the duty of good faith owed by receivers, in addition to the duty to act in a commercially reasonable manner.

