DAVIES

Issue 8

Insolvency Now

Rolling Into 2023: Mild Slumps and Jumps in Insolvency Numbers

Contents

Introduction

The new meme, increasingly used to describe the current state of the economy, is a "rolling recession," rather than the hard or soft landing many commentators expected. In other words, we are experiencing mild slumps rippling through the economy that have the potential to slow inflation without radically impacting the labour market.

In this issue of *Davies Insolvency Now*, we explore what a rolling recession means from an insolvency perspective by examining the 2022 Q4 data, followed by an analysis of two developments we are following, which our clients have asked us to explain.

First, we set out the court-supervised arrangement process under the *Canada Business Corporations Act*, R.S.C., 1985, c. C-44 (CBCA), an increasingly popular tool used to restructure as an alternative to a *Companies' Creditors Arrangement Act*, R.S.C., 1985, c. C-36 (CCAA) process. Second, we provide data-informed insights into the implications of pension reform, which is in the final stages of Senate approval and will see underfunded defined benefit plans receiving super-priority status in insolvency proceedings.

Davies Insolvency Now *is a publication authored by Natasha MacParland, Robin B. Schwill and Stephanie Ben-Ishai that analyzes key trends and developments in the insolvency and restructuring community.*

Q4 2022 Insolvency Data

The Office of the Superintendent of Bankruptcy reported a historically significant (36.8%) increase in business insolvencies (proposals and bankruptcies) from 2021 to 2022. Even more dramatically, the number of CCAA filings increased by 64% for the same period. Receiverships are still experiencing a year-over-year decline, with an unprecedented increase in privately appointed receiverships, as well as in the overall value of assets under receivership. However, this data should be interpreted with caution and in the context of historically low levels of filings throughout the pandemic.

It is too early to suggest that we are on the path to pre-pandemic levels of insolvency filings. At this stage, reported insolvency filing data is best analyzed through a quarter-by-quarter, sector-by-sector and geographic comparison. From that perspective, data is consistent with the rolling recession observed in the economy.

Below, we provide a breakdown of the numbers for each filing option under Canadian bankruptcy legislation, offering a granular analysis of the current and future insolvency landscape.

CCAA FILINGS

General Observations

The number of CCAA filings rose dramatically in 2022, increasing to 41 from 26 in 2021. However, the 2022 number was lower than the 59 total filings in 2020 and never reached the quarterly high of COVID-impacted Q2 2020. The number of CCAA filings rose in each quarter of 2022, from four in the first to 15 in the last.

Sector-by-Sector Observations

The sector with the most filings in Q4 2022 was manufacturing (five of 15 filings), consistent with overall trends. This remained unchanged from Q3 2022 and represents an increase over every previous quarter since Q1 2019.

The other sectors represented in the Q4 data include agriculture, forestry, fishing and hunting; mining and oil and gas extraction; construction; retail trade; transportation and warehousing; finance and insurance; real estate, rental and leasing; management of companies and enterprises; and healthcare and social assistance. There were no identifiable quarterly trends in these sectors.

Regional Observations

Ontario had the most significant quarterly increase, with six filings in Q4 2022 relative to two in Q3. The number of filings also increased in Newfoundland and Labrador, Manitoba and British Columbia. However, there was one less CCAA filing in Québec in Q4 2022 compared to Q3. Overall, Ontario returned to its Q1 2021 filing level, but the number remains lower than in Q2 2020.

BUSINESS BANKRUPTCIES AND PROPOSALS

General Observations

The overall number of business bankruptcies and proposals under the *Bankruptcy and Insolvency Act*, R.S.C., 1985, c. B-3 (BIA) rose by 26% in Q4 2022 relative to Q3 (from an average of 265 to 334 total monthly filings, respectively). However, the total number of filings declined in the last month of Q4, from 361 in November 2022 to 339 in December 2022 (a 6% decline). At the same time, the total number of business bankruptcies and proposals was higher in every month of Q4 2022 relative to the same months in 2021.

Generally, the number of both business proposals and bankruptcies were consistently higher in every month of 2022 versus 2021.

Sector-by-Sector Observations

At the industry level, the most impacted sectors' performance continued to follow historical trends over the last three years. Retail trade insolvencies saw the greatest increase per month and quarter: from 36 in November 2022 to 49 in December. Transportation and warehousing numbers also increased from 19 in November 2022 to 28 in December.

Filings declined in several sectors in December 2022 relative to the previous month, including construction; wholesale trade; information and cultural industries; real estate, rental and leasing; professional, scientific and technical services; management of companies and enterprises; administration and support, waste management and remediation services; educational services; arts, entertainment and recreation; accommodation and food services; and public administration. No declines were seen in December 2021, indicating that this is not a seasonal effect.

RECEIVERSHIPS

Monthly receiverships increased significantly in December 2022, from 19 the previous month to 35. Consequently, Q4 receivership numbers were higher than Q3. The number of court-appointed receiverships in each month of Q4 was higher than for each month of the previous quarter. December and October 2022 numbers exceed the corresponding 2021 numbers.

Overall 2022 receivership numbers were lower than 2021, with 219 versus 286, respectively. The year-over-year decline trend continues.

The declared receiverships asset value was higher in December 2022 than in any prior month of that year.

Not only was the month-over-month increase in privately appointed receiverships from November to December 2022 significant (from three to 15, respectively), but it

also rose meaningfully compared to previous years and well above the December 2021 level (15 versus four, respectively). Starting from 2019, this number is higher than in any previous year, likely due to the use of simpler and lower-cost privately appointed receiverships by a growing number of failing smaller Canadian businesses.

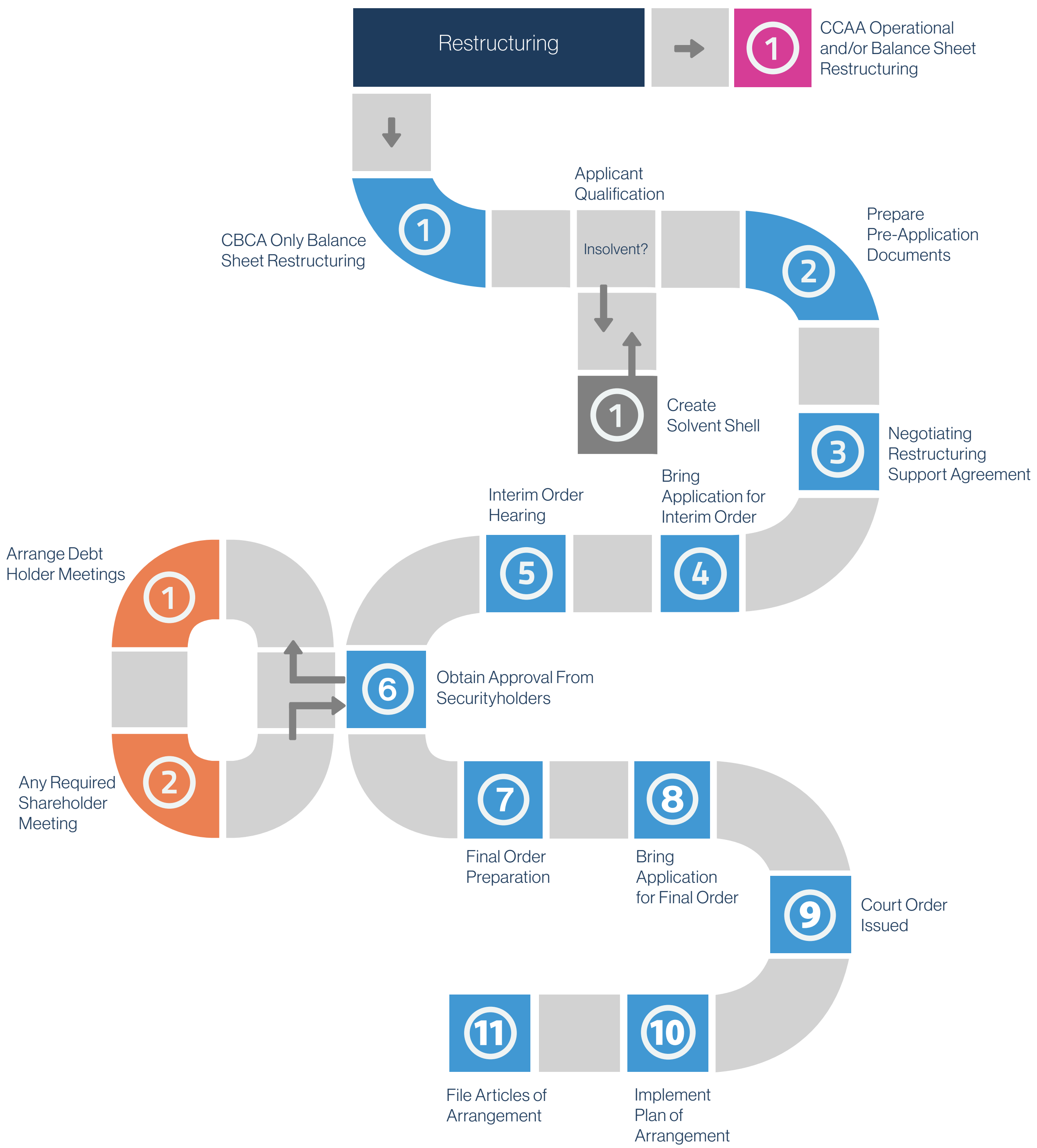
CBCA Arrangements

A process receiving less media attention is the use of corporate law statutes providing for a court-supervised process, where Canadian corporations reorganize both debt and equity and restructure outside of insolvency statutes, such as CCAA. In this section of Davies Insolvency Now, we provide an overview of how an arrangement is completed under Section 192 of the CBCA.

While other provincial statutes provide for arrangements, with limited differences, the increasingly popular approach is using CBCA arrangements. While there are gaps in government data, it appears that CBCA use increased over the previous three years, reaching a plateau over the last 24 months.

CBCA Restructuring Advantage

Click on the relevant squares below to learn more about the steps and advantages of a CBCA Restructuring.



Pension Reform: A Plain Language Explanation of Bill C-228

Should it pass, Bill C-228 (Bill) would amend the BIA and the CCAA. In both BIA and CCAA proceedings, it would ensure claims of unfunded liabilities or solvency deficiencies of pension plans, as well as claims relating to the cessation of an employer's participation in group insurance plans, are paid in priority. It would also amend the *Pension Benefits Standards Act*, 1985, R.S.C., 1985, c. 32 (2nd Supp.) (PBSA), requiring the tabling of an annual report respecting the solvency of pension plans.

Bill C-228 passed second reading in the Senate on December 14, 2022, and is under consideration before the Standing Senate Committee on Banking, Commerce and the Economy. At their last meeting on February 8, 2023, the senators noted that the House passed the Bill in a 318-0 vote and agreed that the Bill included popular aspects of previously proposed amendments and stood a good chance of passing into law.

The Bill provides for a four-year transition period and the senators suggested that, as it did following the 2005 reforms regarding the treatment of unpaid wages, the market would adjust. Countering the argument that companies might be discouraged from setting up defined benefit plans, the sponsor of this Bill noted that the labour market is hot and that companies will use such plans as a differentiator to attract talent.

However, some senators did question whether the Bill would make a difference in practice. The response was that, at this stage, the outcome is unclear because Parliament is not receiving reports on the solvency funding status of pensions, while the Bill would add such a requirement.

The Ontario data on active defined-benefit and/or combination defined-benefit and defined-contribution pension plans we compiled and analyzed supports the limited impact that the Bill will have in practice:

Effective Date	Plan Type	Number of Plans Since Effective Date
January 1, 2003	DB or Combination DB/DC	99
January 1, 2013	DB or Combination DB/DC	40
January 1, 2003	DB	58
January 1, 2013	DB	21

We will continue to follow the progression of the Bill and related data and, if passed, we will provide a detailed summary in a future issue of *Davies Insolvency Now* explaining the practical impact of each aspect of the reforms.

Conclusion

As we look ahead in 2023, we will continue to examine insolvency filing trends in a granular way. We will also continue to follow the solvency of crypto exchanges and the role technology (including ChatGPT and generative AI) plays in future insolvency filings and in practice. We anticipate continued turbulence, but are confident in our measured and data-driven approach to anticipating the risks and opportunities that the current state of financial markets offers to our clients.

Key Contacts

Across novel sectors, Davies has deep expertise in applying our data-driven approach to provide the most appropriate tools for recovery and resolution. Whether providing an early-stage overview or advising on a range of remedial options, we work with you to navigate your unique circumstances and reach your business goals. Please contact any of the individuals listed below or visit our website at www.dwpv.com.

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