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Subject: Nortel Self-Insured Group LTD Benefit Plan Becoming a CCAA Eligible Financial Contract and Deemed Financial Collateral

Navdeep Bains
Minister of Innovation Science and Economic Development
CC: Mark Schaan and Paul Morrison, Ministry of Innovation, Science and Economic Development

At our meeting with Mark Schaan and Paul Morrison at the Ministry of Science, and Economic Development on August 25, 2016, Paul Morrison expressed his concern that our proposal to prescribe a self-insured group long term disability benefit plan as an Eligible Financial Contract ("EFC") would not achieve our desired outcome of immediate top priority full payment of the Nortel self-insured group LTD benefit plan actuarial liabilities owed to the Nortel LTD. Mr. Morrison informed us that a self-insured group long term disability benefit plan did not have a legal term of "financial collateral" and that only the "financial collateral" term of an EFC could be terminated and claimed for an accelerated payment or forfeiture of its full amount. The CCAA permits the termination of the EFC and the determination of its net termination value by netting or setting off obligations between the debtor and counterparties. However, the amount of the net termination value exceeding the financial collateral amount becomes a CCAA creditor claim without priority over other CCAA creditor claims.

I was unaware of this restriction on top priority to just the "financial collateral" of an EFC. I now see that this is indeed the case as set out in the CCAA S. 34(8), 34(9), 34(10) 34(11), which were added to the CCAA at Sept. 18, 2009. These subsections were not there during the Non Bank Asset Backed Commercial Paper CCAA proceedings in 2008-09, wherein I was the court-appointed financial expert for the retail owners of Non Bank Asset Backed Commercial Paper.

Upon discussion of this concern, Mr. Morrison conjectured that it may be possible to define the self-insured group long term disability benefit plan actuarial liabilities as "deemed financial collateral," within the EFC Regulation change that prescribes the self-insured group long term disability benefit plan as an EFC. At the meeting we expressed our enthusiasm for "deemed financial collateral" being the solution for the concern about our EFC proposal not achieving our goal of immediate top priority full payment of the Nortel self-insured group long term disability benefit plan actuarial liabilities.

"Deemed Financial Collateral" is a viable approach for the following reasons:

1. Deemed is an accepted legal term within the Canadian Law Dictionary and U.S. Black's Law Dictionary:

Canadian Law Dictionary Definition of Deem is:
To accept a document or an event as conclusive of a certain status in the absence of evidence or facts which would normally be required to prove that status.

American Black's Law Dictionary Definition of Deem is:
To hold; consider; adjudge; condemn. … When, by statute, certain acts are "deemed" to be a crime of a particular nature, they are such a crime and not as semblance of it, nor a mere fanciful approximation to or designation of the offence.

2. Deemed is already a well-used legal term in both the CCAA and BIA. In the CCAA, "deemed" has 23 mentions. In the BIA, "deemed" has 134 mentions.

3. Financial Collateral in the generic sense is cash, securities, futures agreements, or credit claims that the party owed money in a future contingent event has access to in order to secure performance of a contract. "Deemed Financial Collateral" for the whole self-insured group long term disability benefit plan actuarial liability including the funded portion in a trust and the unfunded portion on the balance sheet of the debtor is consistent with how insurance policies are treated at licensed insurers. Insurance policies (ie., insurance contracts) at licensed insurers have financial collateral in the form of insurance reserves. Upon the winding up of an insurance company, the insurance reserves and any incremental actuarial liability owed for the insurance policies above the insurance reserves are paid at top priority from the liquidated assets before the creditors of the bankrupt insurance company are paid.

4. "Deemed Financial Collateral" is comparable to the concept of "Deemed Trust," where "Deemed Trust" has already been adopted in both the CCAA S. 37(2) and BIA S. 67(3) to permit Revenue Canada to claim debtor's source deductions that rank ahead of certain secured creditors.

5. "Deemed Trust" is used in the Ontario Pension Benefits Act S. 57(4), which sets the precedent for actuarial liabilities owed in the future after the date of the winding up of the group benefit being payable in full and with top priority at the date of wind-up.

Wind up

> 57 (4) Where a pension plan is wound up in whole or in part, an employer who is required to pay contributions to the pension fund shall be deemed to hold in trust for the beneficiaries of the pension plan an amount of money equal to employer contributions accrued to the date of the wind up but not yet due under the plan or regulations.

6. The Supreme Court of Canada in Sun Indalex Finance, LLC v. United Steelworkers, [2013] 1 SCR 271, 2013 SCC 6 (CanLII) agreed that the "Deemed Trust" under the ***Ontario Pension Benefits Act*** (PBA) and, consequently, the statutory priority conferred on that trust under the ***Ontario Personal Property Security Act*** (PPSA) applied to the pension plan's total funding deficiency at the time of the winding up of the pension plan. This decision did, however, determine that the deemed trust under the PBA applies to pension plans being wound up outside of a sponsor's bankruptcy and that it could be superseded by the CCAA judge under the doctrine of federal paramountcy. The CCAA judge can make a finding that the application of the deemed trust under provincial law would frustrate the purpose of the CCAA by causing delay or frustrating the process under the CCAA to restructure the corporation. Such a finding causes the pension deficit to be treated pari passu with the unsecured creditors.

7. "Deemed Financial Collateral" in the new EFC Regulation for self-insured group long term disability benefit plans cannot be superseded by the CCAA judge since federal paramountcy does not apply and the CCAA is a federal law that the CCAA judge specifically administers. In any case, "Deemed Financial Collateral" for a self-insured group long term disability benefits plan would not frustrate the

purpose of the CCAA due to its small dollar amount associated with the usually less than 1% of the workforce affected by long term disability compared to the typical multi-billion dollar bankruptcy estates for the large corporations who can afford to establish a self-insured group long term disability benefit plan.

8. "Deemed Financial Collateral" is comparable to the concept of the Constructive Trust in common law, which CCAA Judge Geoffery Morawetz used in his June 25, 2010 Nortel CCAA decision to award 9 Nortel executive $7.5 million for deferred compensation agreements that had Nortel own Sun Life annuities in its name to finance planned future monthly payments to these 9 executives. The monthly payments ranged from $991 to $31,950.

In conclusion, Mr. Morrison's conjecture to use the terminology of "Deemed Financial Collateral" within the prescription of self-insured group long term disability benefit plans being an EFC is a sound methodology for achieving the goal of immediate top priority full payment of the actuarial liabilities still owed to the Nortel LTD. This approach is an exceptional remedy, in exceptional circumstances, for a deserving case of justice, humanity and compassion for the Nortel LTD. It is also a matter of good Federal Government policy to remove the horrible precedent set by the Nortel bankruptcy and Nortel HWT fraud class action decisions to impoverish Canada's most vulnerable citizens, while executives and bankruptcy professionals are paid billions and the debtor took money from an HWT for its own cash flow benefit prior to bankruptcy.

I will be writing another email on the other concern expressed at the August 25, 2016 meeting about the EFC being prescribed retroactively for the Nortel LTD imposing the risk of a NAFTA arbitration claim for uncompensated expropriation.

Sincerely

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Relevent Sections of Statutes and SCC Decisions Discussed in This Email

CCAA

Subsections 34(8), 34(9), 34(10) 34(11) added to the CCAA at Sept. 18, 2009:
Certain rights limited

- **34 (1)** No person may terminate or amend, or claim an accelerated payment or forfeiture of the term under, any agreement, including a security agreement, with a debtor company by reason only that proceedings commenced under this Act or that the company is insolvent.
- Lease

  (2) If the agreement referred to in subsection (1) is a lease, the lessor may not terminate or amend the lease by reason only that proceedings commenced under this Act, that the company is insolvent or that the company has not paid rent in respect of any period before the commencement of those proceedings.
- Public utilities

  (3) No public utility may discontinue service to a company by reason only that proceedings commenced under this Act, that the company is insolvent or that the company has not paid for services rendered or goods provided before the commencement of those proceedings.
- Certain acts not prevented

  (4) Nothing in this section is to be construed as

- **(a)** prohibiting a person from requiring payments to be made in cash for goods, services, use of leased property or other valuable consideration provided after the commencement of proceedings under this Act;
- **(b)** requiring the further advance of money or credit; or
- **(c)** [Repealed, 2012, c. 31, s. 421]

· Provisions of section override agreement

(5) Any provision in an agreement that has the effect of providing for, or permitting, anything that, in substance, is contrary to this section is of no force or effect.

· Powers of court

(6) On application by a party to an agreement or by a public utility, the court may declare that this section does not apply — or applies only to the extent declared by the court — if the applicant satisfies the court that the operation of this section would likely cause the applicant significant financial hardship.

· Eligible financial contracts

(7) Subsection (1) does not apply

- **(a)** in respect of an eligible financial contract; or
- **(b)** to prevent a member of the Canadian Payments Association from ceasing to act as a clearing agent or group clearer for a company in accordance with the*Canadian Payments Act* and the by-laws and rules of that Association.

· Permitted actions

(8) The following actions are permitted in respect of an eligible financial contract that is entered into before proceedings under this Act are commenced in respect of the company and is terminated on or after that day, but only in accordance with the provisions of that contract:

- **(a)** the netting or setting off or compensation of obligations between the company and the other parties to the eligible financial contract; and
- **(b)** any dealing with financial collateral including
  - **(i)** the sale or foreclosure or, in the Province of Quebec, the surrender of financial collateral, and
  - **(ii)** the setting off or compensation of financial collateral or the application of the proceeds or value of financial collateral.

· Restriction

(9) No order may be made under this Act if the order would have the effect of staying or restraining the actions permitted under subsection (8).

· Net termination values

(10) If net termination values determined in accordance with an eligible financial contract referred to in subsection (8) are owed by the company to another party to the eligible financial contract, that other party is deemed to be a creditor of the company with a claim against the company in respect of those net termination values.

· Priority

(11) No order may be made under this Act if the order would have the effect of subordinating financial collateral.

- 2005, c. 47, s. 131;
- 2007, c. 29, s. 109, c. 36, ss. 77, 112;
- 2012, c. 31, s. 421.

CCAA

Deemed trusts

- **37 (1)** Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be

regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

- **Exceptions**

  (2) Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4)of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision"), nor does it apply in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province if

  - **(a)** that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or
  - **(b)** the province is a ***province providing a comprehensive pension plan*** as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a ***provincial pension plan*** as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

  and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

BIA

- **Deemed trusts**

  67 (2) Subject to subsection (3), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a bankrupt shall not be regarded as held in trust for Her Majesty for the purpose of paragraph (1)(a) unless it would be so regarded in the absence of that statutory provision.

- **Exceptions**

  67 (3) Subsection (2) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4)of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision") nor in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province where

  - **(a)** that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or
  - **(b)** the province is a ***province providing a comprehensive pension plan*** as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a ***provincial pension plan*** as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, notwithstanding any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

Ontario Pension Benefits Act
Trust property

57. (1) Where an employer receives money from an employee under an arrangement that the employer will pay the money into a pension fund as the employee's contribution under the pension plan, the employer shall be deemed to hold the money in trust for the employee until the employer pays the money into the pension fund. R.S.O. 1990, c. P.8, s. 57 (1).

Money withheld

(2) For the purposes of subsection (1), money withheld by an employer, whether by payroll deduction or otherwise, from money payable to an employee shall be deemed to be money received by the employer from the employee. R.S.O. 1990, c. P.8, s. 57 (2).

Accrued contributions

(3) An employer who is required to pay contributions to a pension fund shall be deemed to hold in trust for the beneficiaries of the pension plan an amount of money equal to the employer contributions due and not paid into the pension fund. R.S.O. 1990, c. P.8, s. 57 (3).

Wind up

(4) Where a pension plan is wound up in whole or in part, an employer who is required to pay contributions to the pension fund shall be deemed to hold in trust for the beneficiaries of the pension plan an amount of money equal to employer contributions accrued to the date of the wind up but not yet due under the plan or regulations. R.S.O. 1990, c. P.8, s. 57 (4).

Sun Indalex Finance, LLC v. United Steelworkers, [2013] 1 SCR 271, 2013 SCC 6 (CanLII)

"The wind-up deemed trust provision (s. 57(4) *PBA*) does not place an express limit on the "employer contributions accrued to the date of the wind up but not yet due". Section 75(1)(a) explicitly refers to "an amount equal to the total of all payments" that have *accrued*, even those that were not yet due as of the date of the wind up, whereas s. 75(1)(b) contemplates an "amount" that is calculated on the basis of the value of assets and of liabilities that have *accrued* when the plan is wound up. Since both the amount with respect to payments (s. 75(1)(a)) and the one ascertained by subtracting the assets from the liabilities accrued as of the date of the wind up (s. 75(1)(b)) are to be paid upon wind up as employer contributions, they are both included in the ordinary meaning of the words of s. 57(4) of the *PBA*: "amount of money equal to employer contributions accrued to the date of the wind up but not yet due under the plan or regulations"."

[56] A party relying on paramountcy must "demonstrate that the federal and provincial laws are in fact incompatible by establishing either that it is impossible to comply with both laws or that to apply the provincial law would frustrate the purpose of the federal law" (*Canadian Western Bank*, at para. 75). This Court has in fact applied the doctrine of paramountcy in the area of bankruptcy and insolvency to come to the conclusion that a provincial legislature cannot, through measures such as a deemed trust, affect priorities granted under federal legislation (*Husky Oil*).