Urquhart

Subject: FW: Significance of CCAA/BIA Amendment on Credit Default Swaps Becoming Eligible Financial Contracts V. BIA Amendment for Preferred Status of Employment-Related Claims

Significance of CCAA/BIA Amendment on Credit Default Swaps Becoming Eligible Financial Contracts V. BIA Amendment for Preferred Status of Employment-Related Claims

At the link below I provide documentation on the Bankruptcy & Insolvency Act (BIA) Amendment that was given Royal Assent on November 17, 2007 relating to credit default swap contracts (CDS) becoming defined as eligible financial contracts. Eligible financial contracts cannot be stayed in bankruptcy protection court proceedings and under this BIA Amendment, the CDS creditor claims got super-priority for payment before secured and unsecured creditors, pension fund deficits, long term disability claims and unpaid severance.

http://ismymoneysafe.org/pdf/PrenticeBIAAmendmentonCDSsinABCP.pdf

In my opinion, this BIA Amendment should not have been executed after the $32 billion Non Bank Asset Backed Commercial Paper market froze on August 16, 2007, despite it being put forward in the 2007 Budget prior to the ABCP freeze-up. Surely, sober second thought was in order before the Federal Government would put into effect a BIA Amendment that affected $22 billion of collateral assets associated with $221 billion of CDS contracts within the 20 Non Bank ABCP trusts that were likely to enter bankruptcy protection or bankruptcy proceedings. The Non Bank ABCP CCAA court filing occurred on March 17, 2008.

In chapter 5 of Budget 2007, "A Stronger Canada Through a Stronger Economy", the government indicated its commitment to improving Canada's derivatives market. This lead to Bill C-52, *An Act to implement certain provisions of the budget tabled in Parliament on March 19, 2007*, which was introduced in Parliament on March 29, 2007.

The relevance of the November 17, 2007 BIA amendment for CDSs becoming Eligible Financial Contracts is that this Canadian government was willing to make a BIA Amendment after the Non Bank ABCP market froze for the benefit of the international banks and the CIBC, whereas it is saying it is unable to make a BIA Amendment now in this time of economic crisis for the benefit of Nortel and other bankrupt companies' pensioners, long term disabled and terminated employees. Where were the arguments against retroactive benefits to the international banks and the CIBC, when the June 17, 2007 BIA amendment was made after the ABCP market froze? Why is this government willing to make BIA amendments favouring the international banks and the CIBC, and yet are unwilling to do the same for its citizens now?

How can the current Deputy Minister for Industry Canada rationalize his differential treatment of Canadian citizens versus the international banks when he puts his stamp of approval or rejection on requested BIA Amendments?

Deputy Minister, Industry Canada

Richard Dicerni

May 2006–current
Deputy Minister, Industry Canada

It strikes me that the Deputy Minister of Industry Canada has not based his current opinion on the requested BIA Amendment for preferred status to employment related claims on any research studies. Instead, I wonder if Richard Dicerni is simply accepting the rhetoric of the senior executives of corporations and investment organizations that the BIA amendment for employment-related claims' preferred status will significantly raise the cost of debt when these people also have done no studies on this point.

It is odd public policy to me that the Canadian Government would be of the view that seniors and the long term disabled should be responsible for bailing out corporations that are unable to find debt financing in this time of financial crisis. Also, the BIA Amendment sought is for the cash available in corporations that are liquidating to be given first to Canadian pensioners, long term disabled and terminated employees' severance before the junk bond speculators are paid. These liquidating companies, such as Nortel, are not attempting to raise new debt financing. Ironically, many of the junk bond owners who are helped by not making the requested BIA Amendment for preferred status to employment-related claims are able to profit from bankruptcies due to their ownership of the credit default swaps, which is the same instrument that benefitted the international banks in the Non Bank ABCP fiasco and that reaped the benefit of the November 17, 2007 BIA Amendment. Does Industry Canada only make or not make BIA Amendments according to whether or not there is benefit to junk bond owners and international banks, who largely reside outside of Canada? Surely, this is not so.

Wynne Miles, a retail owner of Non Bank ABCP, said in her attached letter to former Industry Minister Jim Prentice the following:

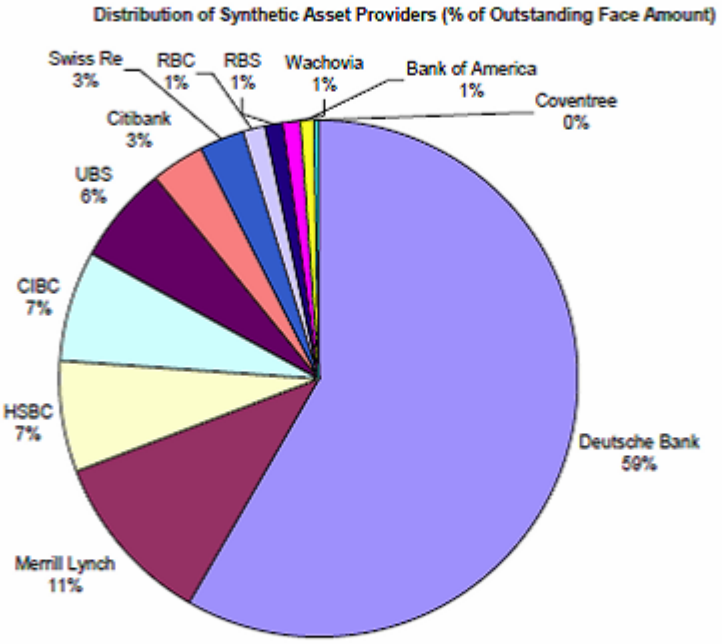
"If you as Minister of Industry had not signed the November 17, 2007 Order in Council, then international CDS counterparties would currently be subject to the same court stay as the ABCP creditors. This would have given both parties equal footing to negotiate with the debtor trusts
for a court approved compromise settlement, rather than allowing the international banks the option of walking away from the CCAA court process to protect their own interests in response to a change in financial conditions. Further, if the November 17, 2007 Order in Council had not occurred, then Judge Colin Campbell presiding over the CCAA proceeding in the Ontario Superior Court of Justice would have the authority to order execution of the ABCP Restructuring Plan by a certain date. The international bank CDS counterparties, as

creditors to the ABCP trusts, would not be free to withdraw from the Restructuring Plan and to take the legal steps entitled within their contracts to collect collateral assets for payment of the amounts owed to them by the trusts.

I question the public interest policy on why CDS were ever placed on the EFC list and therefore exempted from stays in CCAA court decisions. The function of the CCAA is to facilitate compromises and arrangements between companies and their creditors so that the companies may continue operations for the benefit of stakeholders. The CDS counterparties are another class of creditors that should be stayed with all creditors."

The following figure shows which international banks were the beneficiaries of the November 17, 2007 BIA Amendment.

Figure 7: Distribution of Non Bank ABCP Synthetic Assets By Provider (% Face Amount)



Non Bank ABCP Synthetic Assets = Credit Default Swaps
Collateral Assets Face Amount - $22 Billion
Reference Credit Portfolios Face Amount - $221Billion

Source: JP Morgan Report on Restructuring March 14, 2008

Stikeman Elliot LLP was the Canadian legal counsel for the international banks who were the buyers of the credit default swaps contracts sold by the 20 Non Bank ABCP trusts. Stikeman Elliot LLP was also one of the leading proponents for the BIA Amendment applicable to the CDSs.

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The Non Bank ABCP fiasco has cost Canadian investors, ranging from pension funds, government treasuries and individuals $21 billion of lost value at this time. Had the BIA Amendment not been made, it is my opinion there would have been greater negotiating power by the institutional owners of the ABCP to force a greater compromise on the dollar amounts owed under the original CDS contract terms. The consequence of breaking the inane CDS contracts sold by the Canadian Non bank ABCP trusts would have been substantially lower losses on the new notes issued.

Current Marked-to-Market Loss on MAV Notes and Tracking Notes

MAV I & II		Face Amount	Mix	Per FA	MTM Loss
Class A-1		$12,678,937,333	49%	$0.40	-$7,607,362,400
Class A-2		$10,453,119,427	41%	$0.28	-$7,526,245,987
Class B		$1,799,159,970	7%	$0.00	-$1,799,159,970
Class C		$771,068,559	3%	$0.00	-$771,068,559
MAV I & II Notes	Eligible	$25,702,285,288	100%	$0.31	-$17,703,836,916
MAV I & II	Ineligible	$2,288,373,745	36%	$0.17	-$1,895,316,519
MAV III	Ineligible	$1,383,584,444	22%	$0.38	-$860,328,731
MAV III	Traditional	$2,725,505,020	43%	$0.93	-$190,384,369
MAV I, II & III Tracking Notes		$6,397,463,209	100%	$0.54	-$2,946,029,619
MAV I, II & III - All		$32,099,748,497.22	100%	$0.36	-$20,649,866,535

Source: Diane A. Urquhart 28-Oct-09

I do not provide these observations without careful consideration of how the requested BIA Amendment for preferred status to employment-related claims will impact the cost of credit within the Canadian economy. I have studied the matter in two independent research reports that may be read from the following web addresses. My conclusion is that the requested BIA Amendment would impose an increase in the cost of credit overall of 0.05% to 0.26% depending upon the quality of the credit and the term. The impact on the cost of credit is minor due to the small percentage of corporations that file for bankruptcies each year, the incremental loss on default being on top of what is already a high percentage of loss, only about one third of large corporations having a defined benefit pension plan and not all of these having pension plans with deficits. My analysis on the impact on the cost of credit does not take into account bond owners having access to the credit default swap market to hedge themselves against credit default loss in bankruptcies.

Bond Owners Use Credit Default Swaps to Gain, While Pensioners, Disabled and Terminated Employees Told to Share the Pain: Preferred Status in Bankruptcy for Pension, Health and Long Term Disability Deficits and Severance

http://ismymoneysafe.org/pdf/NortelCreditDefaultSwapsandBIAPreferredStatus08042009.pdf

My first analysis on the impact of the BIA amendment of preferred status on the cost of debt was part of the following independent research report that I published on July 6, 2009.

Interventions to Protect Nortel's Canada Estate for Canadians

http://ismymoneysafe.org/pdf/InterventionstoProtectNortel'sCanadaEstateforCanadiansJuly6,2009.pdf

Many senior businessman do agree with my assessment on the cost of credit implications for the BIA Amendment on preferred status for employment-related claims. Three of them have spoken out publicly in BNN interviews at the following webpage.
Jim Gray, former chair, Canadian Hunter Exploration; Bill Dimma, chairman emeritus, Home Capital; and Jim Gillies, professor emeritus, Schulich School of Business.

http://watch.bnn.ca/headline/october-2009/headline-october-20-2009/#clip225668

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