

WHEN IT BECOMES NECESSARY TO REVOKE THE APPOINTMENT OF AN INSPECTOR TO ENSURE THE PROPER FUNCTIONING OF THE PROPOSAL OR BANKRUPTCY PROCESS

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WHEN A BANKRUPTCY OCCURS, THE CREDITORS PLAY A CENTRAL ROLE IN THE ADMINISTRATIVE CONTROL OF THE BANKRUPT'S ESTATE. IN THIS REGARD, THE *BANKRUPTCY AND INSOLVENCY ACT*¹ (THE "BIA") PROVIDES THAT, AT THE FIRST MEETING OF CREDITORS, THE CREDITORS MUST, AMONG OTHER THINGS, AFFIRM THE APPOINTMENT OF THE TRUSTEE AND GIVE SUCH DIRECTIONS TO THE TRUSTEE AS THEY SEE FIT WITH REFERENCE TO THE ADMINISTRATION OF THE ESTATE.² THE CREDITORS WILL ALSO APPOINT UP TO FIVE INSPECTORS TO MONITOR THE BANKRUPT'S ESTATE OR THEY CAN AGREE NOT TO APPOINT ANY INSPECTORS.³

Where inspectors are appointed, the creditors – or even the trustee – will want to ensure that such inspectors act at all times in the general interest of the administration of the estate. The creditors or the trustee can, at law, take various measures to correct the situation if an inspector's action depart from this principle.

ELIGIBILITY AS AN INSPECTOR

The BIA does not specify any eligibility criteria for a person to be appointed as an inspector, except that a person who is party to

a contested action or proceeding by or against the estate of the bankrupt cannot be appointed or act as an inspector.⁴ The legislator clearly indicates that this situation would create a conflict between the interests of the creditors and the personal interest of the inspector. The officers, directors and agents of a legal person that is a party to a contested action or proceeding against the estate of the bankrupt are also excluded.

It often happens that an inspector is the representative of the senior creditor. It is to be noted that this does not create a conflict in and of itself. It is quite the contrary, as stated by the Superior Court in the matter of *Spiridigliozzi (Trustee of)* :

« The process of appointing the inspectors takes place at the meeting of the creditors; it is them and nobody else who appoint the inspectors. The provisions of Section 115 of the Act clearly establish that the amount of votes granted in respect of any questions raised at meetings of creditors is determined according to the dollar amounts of the claims of each creditor. How could it be argued that a creditor with a larger claim should be put aside on the basis of the size of his claim? Is he not the creditor who is the most interested in seeing the administration of the file carried out in a proper manner, to the benefit of all of the creditors? »⁵

¹ R.S.C. 1985, ch. B-3.

² BIA, s. 102(5).

³ BIA, s. 116(1).

⁴ BIA, s. 116(2).

⁵ *Spiridigliozzi (Trustee of)*, B.E. 99BE-1294 (S.C.).

ROLE OF THE INSPECTORS

The inspectors act as representatives of all the creditors and are specifically appointed to monitor the estate of the bankrupt.⁶ Subsections 120(3) and (4) of the BIA impose other duties on them :

« (3) In addition to the other duties that are attributed to them under this Act, the inspectors shall from time to time verify the bank balance of the estate, examine the trustee's accounts and inquire into the adequacy of the security filed by the trustee and, subject to subsection (4), shall approve the trustee's final statement of receipts and disbursements, dividend sheet and disposition of unrealized property.

(4) Before approving the final statement of receipts and disbursements of the trustee, the inspectors shall satisfy themselves that all the property has been accounted for and that the administration of the estate has been completed as far as can reasonably be done and shall determine whether or not the disbursements and expenses incurred are proper and have been duly authorized, and the fees and remuneration just and reasonable in the circumstances. »

Inspectors are required to discharge their obligations for the benefit of the mass of creditors.⁷ They must not place their own interests ahead of their duties and they have the obligation to inform the trustee and their co-inspectors of their personal situation each time there is a risk of a conflict of interest. However, experience demonstrates that in certain circumstances inspectors tend not act in the general interest of the administration of the estate or their actions or refusal to act may become an obstacle to the proper administration of the bankruptcy. Thankfully, the legislator has armed creditors and the trustee with potential corrective measures in such circumstances.

CONTROL MECHANISMS

The BIA provides, on the one hand, that the directions respecting the administration of the bankrupt's estate given by the creditors at any general meeting always prevail over those of the inspectors. In the event that such directions are contradictory, the directions of the inspectors will simply be deemed to be overridden.⁸ The creditors' meeting thus remains the highest authority for decisions relating to the administration of the bankrupt's estate, subject to the exceptional powers conferred on the court when an unjust or unfair situation occurs.⁹

On the other hand, the decisions and actions of the inspectors are subject to review by the court.¹⁰ Thus, upon an application by the trustee or any interested person, the court may revoke or modify any act or decision of the inspectors and may give such directions, permission or authorization as it deems proper in substitution thereof, or send back a matter to the inspectors for reconsideration. However, the courts generally act cautiously in this respect, as stated by the Superior Court :

« The Court must give effect to an application for review of actions and decisions of the inspectors only if such inspectors acted illegally, in bad faith, improperly or contrary to their fiduciary obligations toward the mass of creditors. »¹¹

In the event that the inspectors simply fail to exercise the powers conferred on them, section 118 of the BIA sets out a procedure whereby the trustee may call a meeting of the creditors for the purpose of substituting other inspectors and for the purpose of taking any action or giving any directions that may be necessary.

⁶ BIA, s. 116(1).

⁷ BIA, s. 120(6).

⁸ BIA, s. 119(1).

⁹ BIA, s. 183(1). Also see : *Simpson Place (In re): Druker v. Freed*, [1975] C.S. 765.

¹⁰ BIA, s. 119(2).

¹¹ *Lafrenière (Trustee of)*, B.E. 2001BE-170 (S.C.). Also see : *Nesterenko v. Moquin, Ménard, Giroux, Du Temple inc.*, J.E. 98-314 (C.A.).

As a measure of last resort, where the situation so warrants, a creditor or the trustee may be left with little choice but to file an application with the court to revoke the appointment of the inspector.¹² In the recent case of 9171-7926 Québec Inc. (Trustee of),¹³ the Court agreed to revoke the appointment of the single inspector and appointed a new inspector. In that case, the inspector had initially fulfilled his obligations in a proper manner, in particular by approving all the measures taken by the trustee for the realization of the bankrupt's assets. However, this collaboration deteriorated once the realization was completed, and the inspector refused to finalize the file. The trustee was forced to request that the Court: (i) approve the final statement of receipts and disbursements he had prepared, the dividend sheet and the taxation of the bill of costs; and (ii) authorize him to distribute the proceeds of the realization. It should be noted that the inspector's refusal to cooperate was not premised on his objection to the requests of the trustee per se. The judge noted, and makes the reader implicitly understand, that the reason behind the refusal was rather that the inspector disagreed with the order of priority established by the trustee between two secured creditors, namely, the National Bank of Canada (the "National Bank") and Ferme L.L.R. Inc. According to the inspector, the sums remaining after the realization of the estate should have been paid in priority to Ferme L.L.R. Inc. rather than to the National Bank. The judge further noted that the inspector held an interest in Ferme L.L.R. Inc., while acknowledging that his actions were not tainted by bad faith.¹⁴ However, on the basis of the interest of the mass of creditors, the judge concluded as follows :

« In the present case, it appears that, although he acts in good faith, the inspector confuses his interest in Ferme L.L.R. Inc. with his duties as an inspector. Accordingly, it is in the interest of all the creditors that the Court revokes the appointment of Mr. Luc Roy as an inspector and, as provided under subsection 116(5) of the *Bankruptcy and Insolvency Act*, appoints another in his stead. » (emphasis added)

We note that the Court limited itself to replacing the inspector in accordance with the powers conferred on it by the BIA¹⁵ and dismissed the other conclusions requested by the trustee relating to the approval process.

CONCLUSION

Even if the inspectors are often directly or indirectly related to specific creditors, the BIA requires them to always act in the interest of the mass of creditors, failing which it provides the adversely affected creditors or the trustee with numerous means to remedy the situation.

Creditors should always carefully plan the strategy they will adopt when appointing inspectors. For example, in the above-mentioned case of *9171-7926 Québec inc. (Trustee of)*, the National Bank could have perhaps avoided problems if it had appointed its own inspector, rather than accepting a single inspector representing another important creditor. It may have thereby been able to ensure the proper functioning of the approval process and may have consequently avoided having to exercise this recourse before the court.

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¹² BIA, s. 116(5).

¹³ 2010 QCCS 7085, SOQUIJ AZ-50782127 (S.C.).

¹⁴ BIA, s. 120(6).

¹⁵ BIA, s. 116(5).

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