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1991

**Managing the Insolvency Process  
through  
Effective Consultation**

**"Blueprint for action"**

R.D. Williamson  
Deputy Superintendent  
Restructuring and Proposals

December 12, 1991

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R.D. Williamson  
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## Preface

The task of managing any enterprise through the current period of "**transition**" and safely into the 21st century promises to present new and unprecedented challenges .... as well as opportunities.

This will certainly be the case for the Canadian Public Service!

The pace of change and the need to constantly adapt to global economic pressures (during what will almost certainly be a long period of financial restraint) make this task all the more daunting. Those individuals and organisations who manage to succeed will almost undoubtedly be the ones who thrive and excel on the process change. Their reward will be in meeting the challenge of improvement and adaptation in an increasingly competitive and demanding world.

Those who achieve this success will be those:

### **"Who can see beyond the practical... to the possible"**

This Report outlines a "**Blueprint for Action**" by the those who are responsible for overseeing Canada's insolvency system during this difficult period. It attempts to do so in a way which responds to the challenge before us and overtly seeks to "**reposition**" the Office of the Superintendent of Bankruptcy in a new and modern context.

It offers a bold "**shift**" in both emphasis and approach which, we believe, is consistent with the initiatives established by PS 2000 and is also in keeping with the more general trends we find in effective business management philosophy today.

It seeks to place the "**management**" of the insolvency process in a new light with a commitment to four basic principles.

1. **Consultation**
2. **Partnership**
3. **Efficiency and**
4. **Quality service**

We make no excuses for recommending a sharp break with the past and in advocating the need for radical solutions in the future.



## The Governments Commitment to Partnership and Consultation

"The word partnership appears frequently in this document and will be heard often during the consultations. Our success will require the cooperation of many, some of whom have profound differences"

"Discussion, consensus and partnerships will allow us to improve our competitiveness and learning."

"Canada's future prosperity.... depends on the willingness of Canadians to develop a new sense of partnership"

"The willingness of Canadians to work together in a wide range of partnerships - within and between firms; between management and labour; among all levels of government and between the public and private sectors - will serve as the mortar."

"A greater degree of partnership among the principal stakeholder in the private and public sectors is required to achieve a more innovative... economy."

Extracted from the Federal Government's  
Consultation Paper

"Prosperity Through Competitiveness"

November 1991

**The Government's Commitment  
to  
The Renewal of The Public Service of Canada  
PS 2000**

"These challenges call for a Public Service....that is much more open in its relationship with Canadians and much more flexible in its internal procedures. A new consultative service-oriented culture needs to be created."

"A fundamental rethinking is necessary of what the Public service does and the way it does it."

"The government wants to create a client oriented Public service a major change since the Public service has not been used to regarding Canadians as clients"

"Consultation and partnership are increasingly important aspects of service to Canadians"

"Until recent years the policy making process was essentially internal to government.... There is a growing realization that government is not the only locus of responsibility for solving particular problems and issues"

Extracted from the Federal Government's Synopsis  
on Public Service Reform

December 1990

**The Government's Commitment  
to  
The Business Government Executive Exchange Program**

"Partnership and cooperation between the business community and the Federal Government will assure Canada's continued economic prosperity well into the 21st century."

"For anyone who thrives on challenge and change the 1990's will be an exciting era.... the future can only be achieved if business and government establish a closer working partnership."

"We need to build a stronger spirit of cooperation - a partnership of excellence."

Extracted from the Prime Minister's  
Message to the Executive Exchange  
Program for 1990



## Introduction

It has become a well accepted fact of life that organizations (of all types) will spend a considerable amount of their time and energy in establishing a formal "**Mission Statement**" and in crafting a "**vision**" to which they, their employees and their clients can subscribe. A statement which serves as a clear, self explanatory and motivating commitment.

The emphasis of management has shifted in recent years from "**control and procedure**" to "**effective execution**". To this end, the Mission Statement has developed as a means for organizations to address the demand:

- for simplification and personalisation
- as a means to focus the attention of constituents
- for differentiation in a demanding market
- as a means to gain support from diverse groups and
- to ensure there is common interest and purpose

As we move into the next century, the pressures being placed on organizations are unlikely to subside and the complexity under which we will all be forced to operate will inevitably grow. In this kind of rapidly changing and uncertain environment, only those organizations who are in tune with the world around them and who can effectively communicate with their constituents (and/or clients) will survive. Furthermore, only those who take the time to develop a well thought out and coherent "**blueprint**" for action will even be given the opportunity.

The challenge is to seek out the new "**paradigm**" and find ways to manage nothing less than a "**quantum shift**" in thinking and practice.

In the specific case of the Canadian bankruptcy and insolvency system these general "**environmental**" factors will be supplemented by some unique pressures and realities.

These include:

- the likely continuing restraint under which Government will be forced to operate (from both a financial and a manpower point of view)
- the broad management and cultural influences which are part of the PS 2000 initiative and
- the changing nature of relations with the Provinces

Finally, we are about to enter the long awaited (but uncharted) territory of modernized insolvency legislation in the "**post**" Bill C-22 era.

This will provide it's own challenges but also the opportunity to establish a mechanism to ensure the legislative development process is sustained and that future amendments to the legislation do not suffer from the same divisive, unhealthy and protracted circumstances which have led to the sad history of insolvency reform in the past.

## Mission Statement

To this end, it is both appropriate and necessary for us to establish a theme or "**Mission Statement**" that fully addresses this new set of circumstances and more accurately communicates a "**vision**" of the insolvency process and its purpose.

One such statement might be:

**"Managing the insolvency process  
through  
effective consultation"**

This theme has several attractive attributes which address the key issues and concerns we face today, as well as those we are likely to face in the future.

These include recognition of the importance we must place on:

- |                 |                                                                                                                                                                                                                                                                                                                                                                                                                                                          |
|-----------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Managing</b> | <ul style="list-style-type: none"><li>- which helps to project a more "<b>pro-active</b>" leadership role (on the part of the Government) and one which shifts emphasis to "<b>action</b>" rather than "<b>re-action</b>" and to being in control of events, rather than a witness to them.</li><br/><li>- It sets a professional standard for a new, wider "<b>market oriented</b>" approach on the part of the Superintendent of Bankruptcy.</li></ul> |
| <b>Process</b>  | <ul style="list-style-type: none"><li>- a recognition that bankruptcy is not an end in itself, but rather only one part of a more "<b>all encompassing</b>" phenomenon within the</li></ul>                                                                                                                                                                                                                                                              |

much broader context of financial distress

- Effective** - an acknowledgment of the increasing need for any Government process or program to be seen to be worthwhile and efficient and for its basic value to be easily measured from a productivity standpoint
- Consultation** - reflecting the role of the Government, as "**custodian**" of the insolvency process, but also as the "**facilitator**" for greater private sector involvement and with joint responsibility for the system, its integrity and its professionalism.

As we proceed into this "**new era**" there is a unique opportunity for us to significantly redefine the role we wish to play and the way we choose to play it!

In short, there is an opportunity to make ourselves more "**relevant**" to the world around us and more "**professional**" in our dealings with the private sector.

This implies recognition of some basic "**guiding principles**":

- a responsibility for the management of the process
- a much wider vision of the agenda and
- a true commitment to new and sincere forms of partnership with the private sector



## Consultation - Defining the Agenda

At the very "**core**" of this process of change and rejuvenation, is a commitment to the need for ongoing consultation with the private sector and to the negotiation of "**service contracts**" with our constituents. A "**contract**" wherein our role is defined, agreed upon and the terms of the partnership set.

This represents a new and progressive approach to our dealings with the private sector but one which is totally consistent with the direction in which the Government (and the Public Service in particular) is committed in moving.

It also represents a redefinition of the traditional role played by a supervisory or regulatory function and attempts to move it into a framework better suited to the 21st century.

Webster's Dictionary defines "**consultation**" as:

**"The act or procedure of consulting....a conference at which advice is given or views are exchanged"**

It goes without saying, this "**act or procedure**" must be effective if it is to have any credibility at all. Achieving that credibility will be the toughest part of the assignment, particularly as there will inevitably be some initial scepticism on the part of the "**stakeholders**" and possibly even some resistance to the idea of establishing a new partnership.

To help alleviate these problems, there are four basic rules which must be faithfully followed.

1. There must be a **set and known** procedure - not just an "ad hoc" series of occasional, informal meetings.
2. The emphasis must be on **sustained commitment** and an **established** format.
3. If we are truly seeking advice - then, there must be a **willingness to accept it and perhaps even more significantly, to act** upon it.
4. Finally, **all** of the parties must be prepared to hear **all** of the views - even those that are **unfavourable**.

Strict adherence and belief in these rules is an absolute prerequisite for any effective consultation process. Failure to accept and enact these rules will inevitably lead to the failure of the process. There are no short cuts to achieving the full benefits and there can be no compromises to the basic principles.

## Consultation - Why bother?

Several leading management consultants and noted business "**gurus**" have written and lectured extensively on the consultation, partnership and alliance process. They have helped set the concept within the framework of changing times and global circumstance.

In recent years, the "**private sector**" has sought answers to the many problems which increased competition and new technology have placed on both management structures and philosophy.

They have passed through the "**productivity**" and "**excellence**" phase and businessmen now find themselves rapidly converting to the latest "**organizational religion**". Almost without exception, they have become ardent followers of the new generation of management philosophers who are promoting the twin concepts of "**quality service**" and "**networking**" as the ultimate answer to success in the 1990's.

While the Public Service may "**lag**" the private sector in respect of the application of these practices .....it does not do so by very much!

There are clear signs the management and organisational agenda for the Public Service of Canada is moving in the same direction as the private sector. The Government has made it quite clear (in number of different ways), that it wishes to create a new type of "**partnership**" between the public sector and the private constituencies it serves.

The emphasis on these "**partnerships or networks**" is founded on the belief they are a necessary ingredient in attempting to achieve what will be the real measure of success in the future, namely:

**"Ensuring superior execution in a volatile environment"**

Indeed, governments everywhere have known for some time (and certainly for a lot longer than the corporate world) that there is both wisdom and benefit in the formation of strong alliances or partnerships in a complex and uncertain world.

While government has know this to be true in the conduct of foreign affairs, there appears to have been somewhat of an "**allergy**" to the loss of control that partnership might seem to imply when it comes to a regulatory or supervisory function like bankruptcy.

It is this very fear we must seek to overcome because there is simply no longer any future for a Public Service that is not totally committed to a sense of partnership.

## Reshaping Organizations - for results

One of the leading experts in the field of networking, partnership and empowerment is Ram Charan, an American based consultant who has advised many top global enterprises who are struggling with the process of cultural and attitudinal change. Some of his insights have direct application the process we are about to undertake.

### Reshaping Organizations - for Results

Networks imply a complex set of external relationships.... a web of alliances and joint ventures

Networks mean informal ties..that work across functions.. and manoeuvre through bureaucracy

A network reshapes how and by whom decisions are made

Membership criteria are simple but subtle....select group(s) who by virtue of their ...skills and judgement, personal motivations and drive ....and positions at the juncture of critical information flow ...are uniquely equipped to shape and deliver on the ...strategy.

The foundation of a network is in its social architecture.. which differs in important ways from organizational structure

Social architecture does not imply ... harmony. The single most important role is to surface and resolve conflict - to identify legitimate disagreements ...and to make difficult trade offs quickly and skilfully.



## **The pressures for change:**

There are at least four levels of change currently influencing the business environment in general and the Public Service in particular. Each is placing its own severe pressure on the insolvency system to react.

These include:

- the "micro" financial and structural pressures
- overall "market" and societal pressures and
- the "macro" economic realities and
- the process of corporate/organizational renewal

## **The "micro" pressures**

In the case of the Government, the micro financial and structural pressures are converging more rapidly than elsewhere.

They are influencing the system in unique ways, well beyond those found in the private sector and they are placing unprecedented demands on the Public Service.

These factors include:

- the severe financial and budgetary pressures under which the Public Service is likely to have to labour for many years to come
- the manpower constraints (in both numbers and qualifications) which arise out the above
- the public's demand for less.....but more effective government
- the painful process of re-defining responsibility between various levels of government

All of this places a serious burden on the Public Service and it is forcing a total (and fundamental) re - evaluation of the way in which any Public Service function is conceived and ultimately executed.

This certainly applies to the bankruptcy and insolvency process!

Indeed, in light of the regulatory changes which will be brought about as a result of the passage of Bill C-22, the need for this re-evaluation is probably even more compelling than in many other areas of Government.

### **The broad market pressures**

At the next level of "**pressure**" we find a variety of market or societal issues which are increasingly coming to bear on the insolvency system as they are, in fact, on all other Government regulated or supervised functions.

These include:

- continued pressure towards "**privatization**"
- growing demands for "**de-regulation**" and or "**self-regulation**" and
- the importance of international harmonization

The realisation that Government can not (and perhaps should not) strive to be "**all things to all people**" is forcing an examination of the many ways in which services can either be made "**self financing**" or perhaps even passed over to the private sector.

In the professional insolvency world, there is a strong case which can be made for the Trustee community to increasingly come under the supervision of its own regulatory body, be it the CIA or some variation thereof.

Over time, this is a subject which will have to be addressed.



## **The macro - pressures**

Yet another level of "pressure" (and one quite specific to the insolvency process) arises out of the "macro" economic climate we face. These factors place their own pressure on the insolvency process and together they will dramatically impact the nature, volume and substance of the insolvency process.

These factors include:

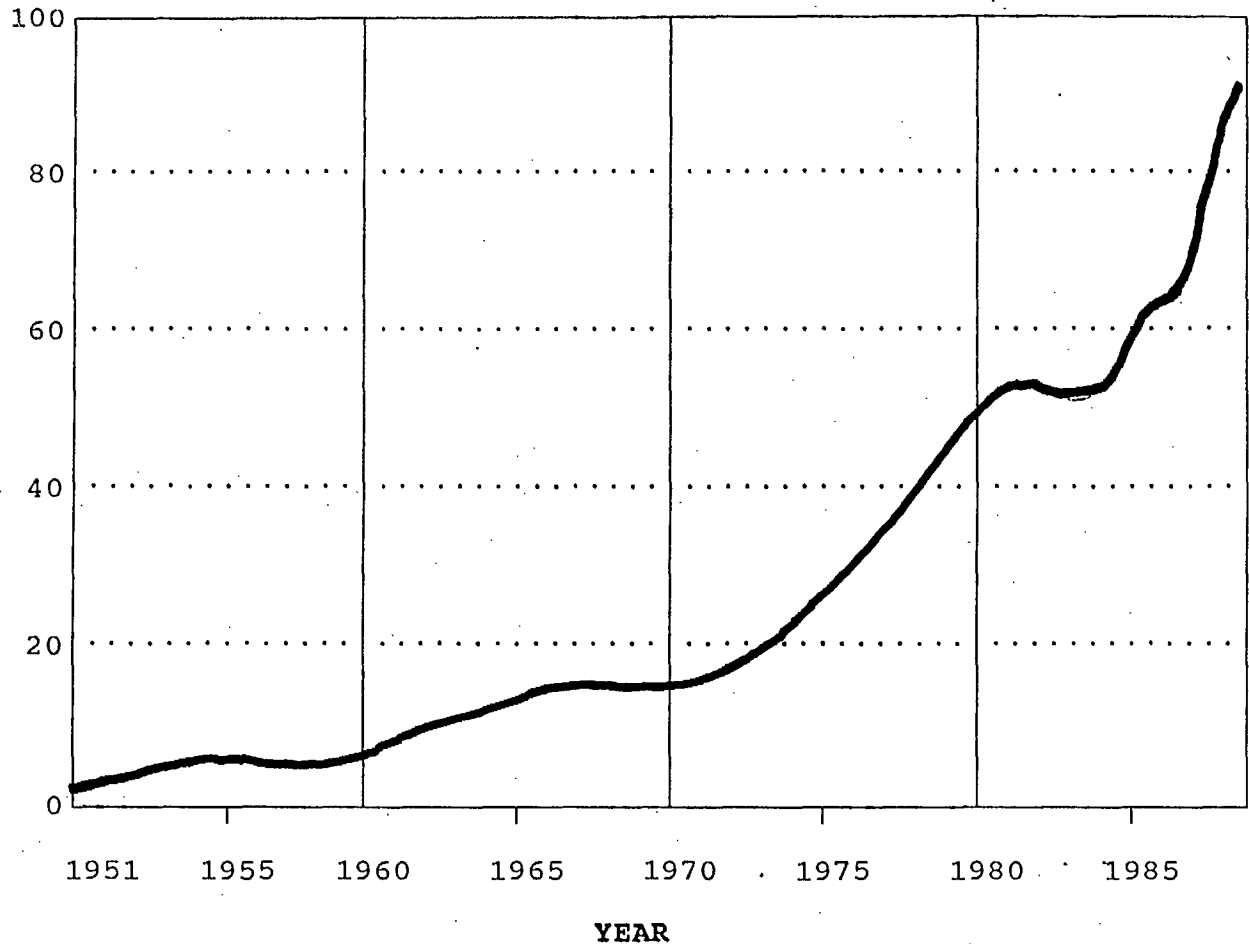
- a continued rise in both consumer and business borrowing/debt levels
- the increasing sophistication of the lending market
- enhanced levels of competition and innovation amongst financial service institutions
- the continuing emergence of new, non traditional financial service
- a resulting increase in the level of pressure being placed upon the consumer and small business and
- a continuation of the difficult and painful process of restructuring the business environment and establishing Canada's new role within the global (and particularly North American) economy

These factors are irreversible. They will continue to place extraordinary pressure on a system which, itself, needs to be more closely integrated with the Government's own economic prosperity agenda.

The manner in which we treat businesses who run into financial difficulty and the system we apply to their administration are both important (but not yet well understood) components of the wider economic challenge.

## Factor 1

### Rising levels of Consumer Credit



**TOTAL CONSUMER CREDIT OUTSTANDING, CANADA 1951-1989**

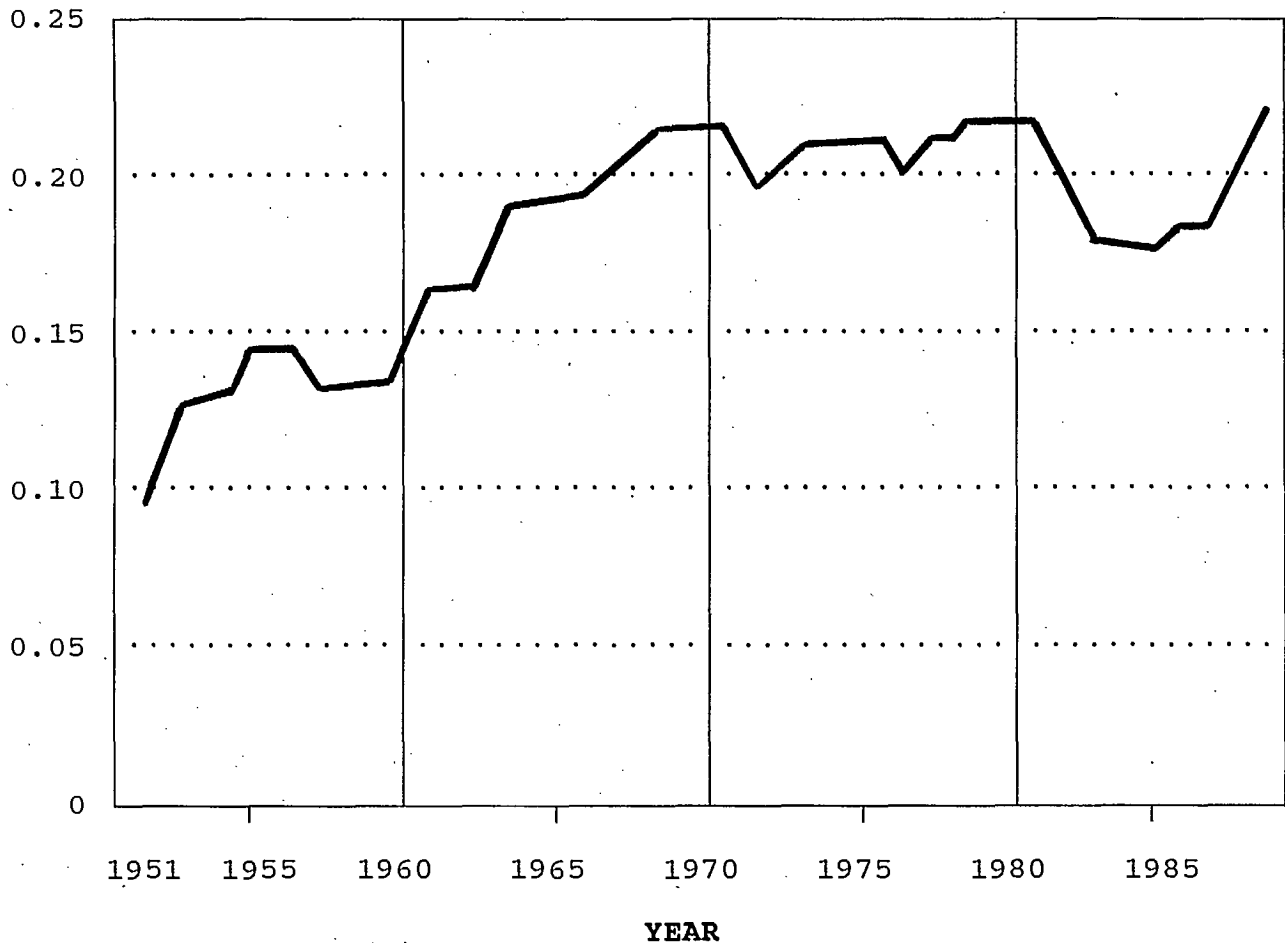
Source of data: Bank of Canada Review

As these figures indicate, there has been a consistent upward trend in Consumer Debt levels since the 1950's. However, the trend in the post recession period of 1983-1987 is particularly disconcerting.

The trend would support economic theory which attests to the growing social acceptance of debt in Canada, as we have become an even more "consumer driven" society.

## Factor 2

### Rising Consumer Debt Ratios



**RATIO OF TOTAL CONSUMER CREDIT OUTSTANDING TO PERSONAL  
DISPOSABLE INCOME, CANADA, 1951-1989**

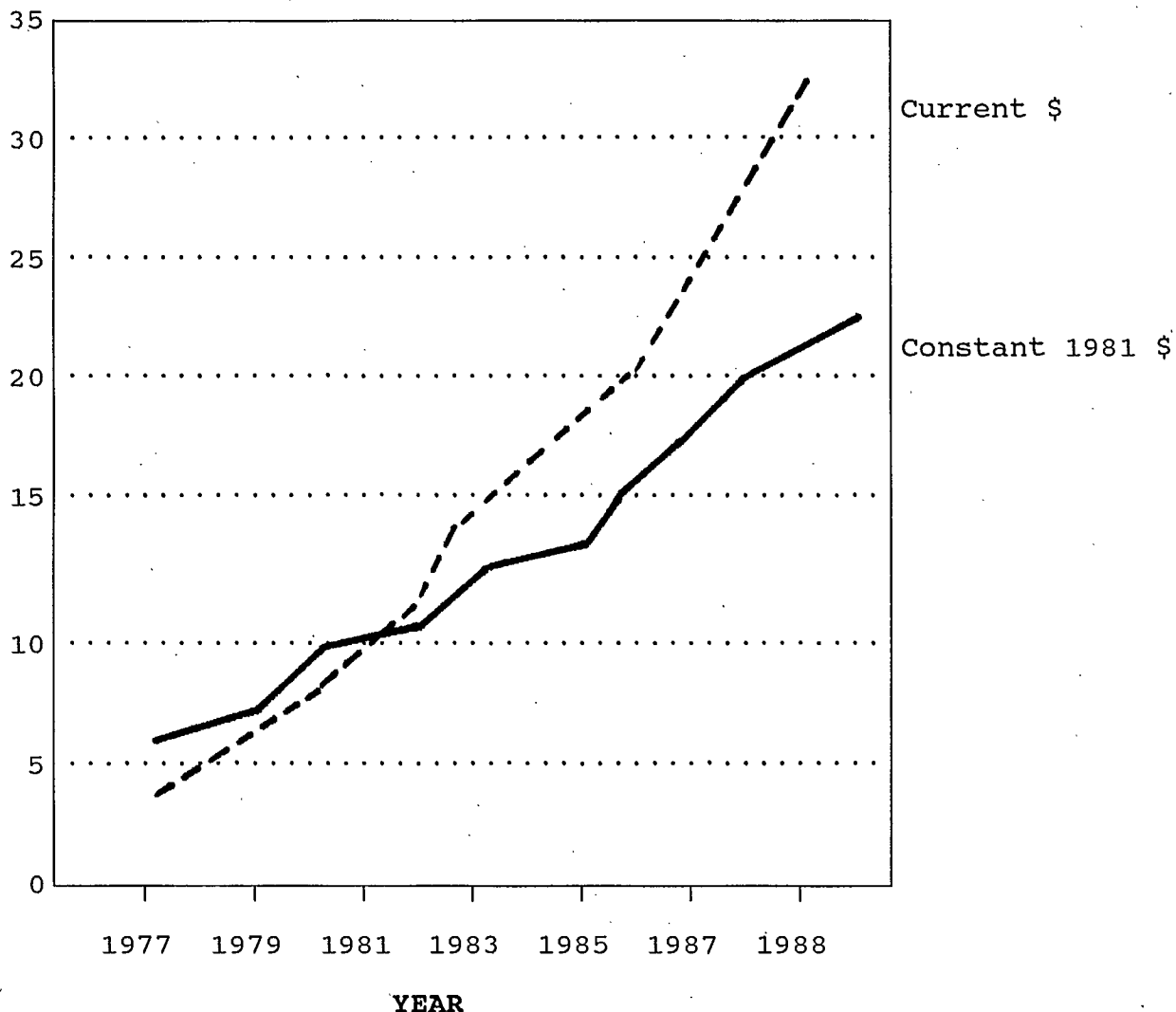
Source of data: Bank of Canada Review

Combined with a rise in Consumer Debt has been a similar rise in the Debt Service Ratio. While it is true the ratio declined in the 1980-1983 period, the "core" level is more than double that of 30 years ago.

This has had the impact of making the consumer more vulnerable to interest rates movements and the economy overall and more likely to incur financial distress for reasons directly outside their own control.

### Factor 3

#### Expanding Credit Card Markets



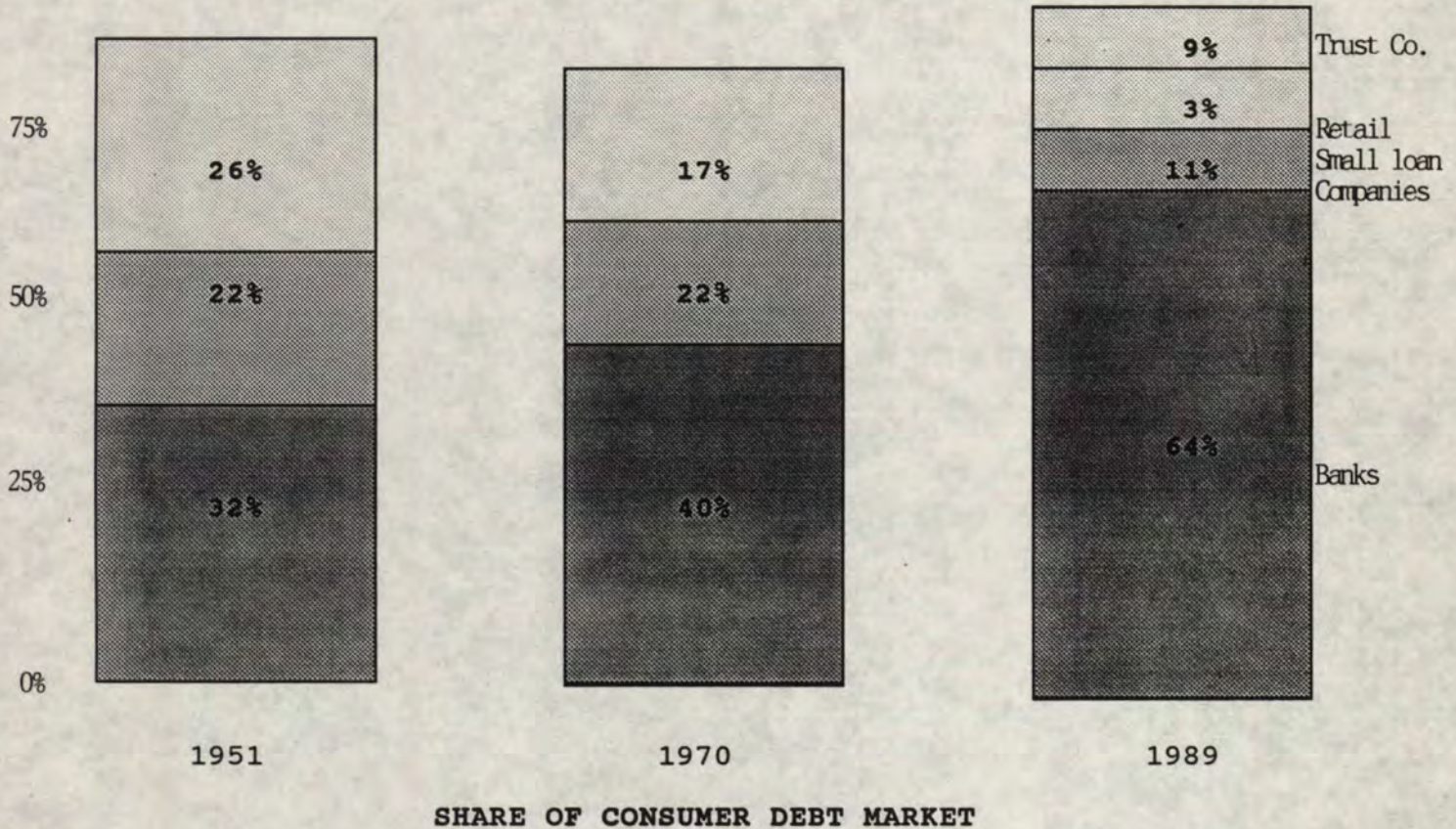
#### TOTAL SALES USING MASTERCARD AND VISA

Source: Consumer and Corporate Affairs

The availability of credit cards and their acceptance in the market amongst consumers is often blamed for the rise in personal bankruptcy. There is certainly evidence to indicate that Credit Cards have enjoyed a boom in popularity during the past 15 or so years.

## Factor 4

### Increased competition amongst financial institutions



Source: Personal Finance for Canadians Prof. K. Brown

The financial services industry has undergone a monumental transformation in recent years and the process continues. The level of competition amongst the major providers of credit is acute and the emergence of new players is likely to continue.

In Canada, the major banks provide the majority of consumer credit and their importance is growing in both dollar terms and market share. The changing role of credit cards is a direct factor

Factor 5

Aggregate Small Business Balance Sheet Ratio's

Percentage of Total Debt

|       |       |
|-------|-------|
| TRADE | 46.1% |
| BANKS | 28.4% |
| OTHER | 25.5% |

Source: Banks and Small Business: UWO Study, 1991

A much misunderstood and certainly under appreciated factor in the financing of Canadian business is the extent to which "Trade Credit" is extended and the fact its share of the typical debt profile is larger than that of bank loans.

This unregulated and unsupervised financial market is amongst the most important and most innovative in the country. The granting of what amounts to unsecured, short term finance on an inter-corporate basis is one of the major cylinders for the smooth running of the economic engine.

The losses incurred by "the trade", in bankruptcy, are significantly larger than those incurred by the banks and the other financial service institutions.



## Options and environment

These few, very basic statistics are meant to provide an overview of the "macro" economic events taking place around us. These events will take place regardless of changes to the insolvency legislation or the way in which we choose to manage the process.

They foretell a continued, lengthy and painful period of economic instability, fundamental economic restructuring and attitudinal adjustment. This almost certainly means mounting levels of pressure on the system and on those members of the Public Service who are involved in the management of the insolvency process.

In blunt terms, even if the bankruptcy numbers decline in the foreseeable future, it is likely the system will be faced with:

- permanently higher "core" levels of financial failure
- larger and more complex business failures
- a generally more adversarial environment
- far greater levels of insolvency litigation and
- more cases of financial failure with international and/or cross border implications

There is every reason to expect that the pace of change will require us to be in an almost continuous process of legislative evaluation if we hope to ensure the insolvency regime keeps pace with the world around it.



We can choose to face this new and emerging reality in several different ways .... What we cannot afford to do is ignore the need to meet the challenge head on.

We can attempt to:

**Do more.... with more - although it seems unlikely resources (of any type) will become more readily available**

We can attempt to:

**Do less..... with less - which is certainly a possibility**

We can attempt to:

**Do more..... with less - which the "public" might like**

**or**

We can attempt to:

**Do more ..... in new and more productive ways**

This last choice would seem to be the only justifiable option.

It is, therefore, the one we are promoting and the only one which can hope to produce the results necessary to meet the challenge.

While it may appear to be the "**highest risk**" alternative and the most difficult to execute, it is the only one with a certain, long term "**payoff**".

In the relentless search to "**Do more, in new and different ways**" and to do so in an increasingly more cost effective manner, the corporate world has chosen to place its emphasis on the principles embedded in such widely accepted Quality Programs as the Baldrige Awards in the U.S.A. (and its various national counterparts elsewhere, including Canada).

Advocates of the Baldrige approach would claim:

**"(it) has become the most important catalyst for transforming ...business and more than any other initiative, public or private, it has reshaped .... thinking and behaviour".**

The basic philosophy of the Baldrige approach can equally be applied to the Public Service and to our efforts to create a revitalised and forward thinking insolvency management process.

### **The Baldrige Categories**

- 1. Leadership**
- 2. Information and analysis**
- 3. Strategic Planning**
- 4. Resource utilisation**
- 5. Quality assurance of services**
- 6. Results**
- 7. Client satisfaction**

## **Partnership for change - The Constituents**

In order to better understand the need for change (as well as the reasons and pressures which have conspired to make effective consultation the only answer to the future effective management of the insolvency system) we must look at the "**constituency or stakeholder universe**" as it exists today..... and as it will likely exist tomorrow.

In doing so, we must be prepared to accept two philosophical cornerstones which support the entire consultation process.

### **Partnership and participation!**

That is to say ..... a **partnership** ... in which there is an agreed upon and shared sense of responsibility and .... **participation**..... that is both complete and energetic.

To manage the overall process effectively we must therefore:

- **seek out the widest range of possible "partners"**
- **ensure adequate and responsible representation by all of the various stakeholders**
- **fully recognize the diversity (and perhaps even conflicting interests and concerns) of each group and**
- **strive to create a true partnership amongst equals**

The role of the Government in this process (and more specifically the Office of the Superintendent of Bankruptcy) should be to act as the "**facilitator**" for the creation of an open and constructive dialogue, amongst all the parties, leading to the development of new private sector initiatives tailored to the specific needs of the community at large.

## Keys to Successful Collaboration

1. Treat the collaboration as a personal commitment. People make partnerships work.
2. Anticipate it will take up management time. If you can't spare the time, don't start it.
3. Mutual respect and trust are essential. If you don't trust the people you are negotiating with, forget it.
4. Remember that both partners must get something out of it. Mutual benefit is vital. This probably mean you will have to give something up. Recognize this form the outset.
5. Make sure you tie up a tight "contract". Don't put off resolving unpleasant or contentious issues until "later". However, once signed, the contract should be put away. If you refer to it, something is wrong with the relationship.
6. Recognize that during the course of a collaboration, circumstances and markets change. Recognize your partner's problems and be flexible.
7. Make sure you and your partner have mutual expectations of the collaboration and its time scale. One happy and one unhappy partner is a formula for failure.
8. Get to know your opposite numbers at all levels socially. Friends take longer to fall out.
9. Appreciate that cultures - both geographic and corporate - are different. Don't expect a partner to act or respond identically to you. Find out the true reason for a particular response.
10. Recognize your partner's interests and independence.
11. Even if the arrangement is tactical in your eyes, make sure you have corporate approval. Your tactical activity may be a key piece in an overall strategic jigsaw puzzle. With corporate commitment to the partnership, you can act with the positive authority needed in these relationships.
12. Celebrate achievement together. Share elation, you will have earned it!

## The partnership universe - as it exists

At the heart of our historical relationship with the professional insolvency world we find the 600 or so **Trustee's in Bankruptcy** who are licensed by the Superintendent. In the past, these professionals have (for the most part) been the only ones actively involved with the Government in the insolvency area. Their professional body, the **Canadian Insolvency Association (CIA)**, has similarly been the major private sector organisational counterpart. The Joint Committee on Bankruptcy has, therefore, become the primary forum for interchange with the profession.

However, as things have developed, the professional insolvency world in Canada has now grown to include three separate bodies, each of whom can claim to have a legitimate interest in bankruptcy and/or insolvency as a specialized profession.

These include:

|                                             | <u>Members</u>       |
|---------------------------------------------|----------------------|
| <b>The Canadian Insolvency Association</b>  | <b>Trustees only</b> |
| <b>The Canadian Bar - Insolvency Branch</b> | <b>Lawyers only</b>  |
| <b>The Insolvency Institute</b>             | <b>By invitation</b> |

The emergence of these separate "**associations**" is a recognition of the fact (particularly since the 1980 recession) that the insolvency world has been forced to widen its scope in order to include more than just the accounting profession.

It is also fair to assume that the number of interested professionals or para-professionals will increase over time. Currently, there are a number of "**para-legal**" groups examining the possibility of actively perusing "**Proposal work**" under the new Act. Similarly, there are Debt Counsellors and Provincial Departments who can also claim to have an operational interest.

## Influences on the Existing Partnership

During the past several years the CIA has been subject to various internal pressures and has been attempting to deal (somewhat unsuccessfully) with the need to represent both the "**sole practitioner**" who chooses to specialise in Consumer Bankruptcy work and the "**larger, multi-discipline firms**" who conduct Receivership, CCAA filings, Corporate Reorganizations and workouts, as well as traditional bankruptcy work.

Consequently, it might be fair to say the CIA is itself now fragmented into at least two separate constituencies, the corporate and the consumer.

Without wishing to enter into an analysis of the strengths, weaknesses or merits of each of these three (or four) groups, suffice it to say it is no longer appropriate or desirable for the Government to deal with the CIA as the sole or unanimous voice for the entire professional insolvency world.

This development or trend towards fragmentation or growth in the "**industry**" has occurred for a number of reasons and points out the need for us to review the manner in which we interface and consult with the private sector professionals.

These reasons include:

- the significant rise in the "**core level**" of Consumer bankruptcies (since the early 1980's) which has led to a rise in the available "**market**" for the services of specialized Consumer Bankruptcy Trustees
- an appreciable increase in the number of "informal reorganizations" (including CCAA filings) for financially distressed companies which has led to the rise in the role of the lawyer as a "**reorganization**" specialist
- the "**complexity**" of the larger corporate bankruptcies and "**workouts**" which has led to the need for more sophisticated linkages between senior legal and accounting professionals and their clients .....the large financial institutions

In short, there have been some very good and rationale "**market driven**" reasons for the continuing development of the professional insolvency community. In turn, these require an appropriate response from the Government, both as regulator of the process and as custodian of the public trust in this area.

It would not appear the existing "**partnership**" with the CIA has been able to keep pace with these changes.

## The partnership universe - as it should be

While the relationship or partnership between with the professional insolvency community (lawyers and Trustees) and the Government is vital, an equally important constituency is the credit granting community and their clients .... the borrowers.

Each of these groups has a unique interest in the nature and workings of the insolvency process and beyond that, they have a direct financial interest or exposure which they naturally wish to secure, protect and manage.

In the same way as it is no longer appropriate to deal only with the CIA (as the sole representative for the professional insolvency world) it is no longer appropriate to think only of the large banks when it comes to the financial services sector.

The number and diversity of players in this sector has grown in recent years and is expected to continue to do so. The level of sophistication, segmentation and specialisation in the provision of both corporate and consumer debt will continue to grow and the financial stakes will become larger and more complex to manage.

Indeed the interests, attitudes and concerns of each group of credit grantors will vary substantially and the complexity of dealing with this sector can not be underestimated. The fact of the matter is, it is only right that those who put their money at stake should have a greater direct voice and involvement in the insolvency process... not as "**single issue**" lobby groups, seeking to protect their own position..... but as part of a national, multi-discipline professional forum.



There are a least 7 major sectors in the financial services world with whom we should deal (and no doubt several sub-components of each as well).

In approximate order of size and influence this are the:

1. Banks
  - Domestic (Schedule A)
  - Foreign (Schedule B)
  - Offshore
2. Trust Companies
3. Finance companies
4. Non-financial vendors
  - Automotive finance
  - General merchants
5. Credit cards
  - General... Visa, MC etc.
  - Specific.. Sears etc.
6. Investment banks
7. Unsecured trade creditors

The following section of this Report attempts to deal with this topic in greater detail and explain the trends and influences which are impacting upon credit grantors in general.

## **The remainder of the universe**

However, it is equally important we not overlook the remainder of the insolvency universe who, although they do not have a financial or legal stake in the process, nevertheless do have interests of various sorts.

This is a sector which includes a diverse number of talents and unique perspectives. It would be shortsighted and against our best interest if we were to exclude any of the following groups from active involvement in the consultation process.

**The Credit Bureaus** In their capacity as the only independent "record keeper" for the financial community

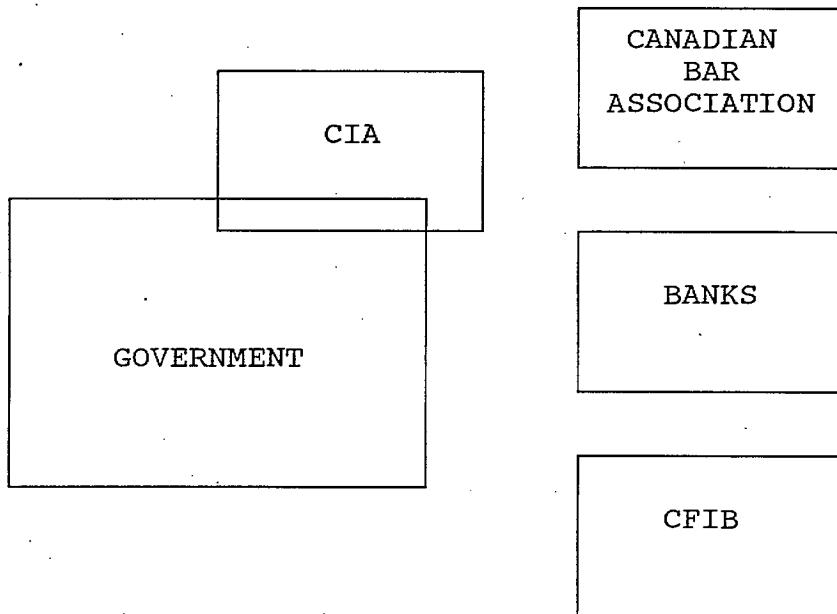
**The Academics** In their capacity as both:

- unbiased analysts and researchers of trends and developments and as
- educators of professionals in business and finance

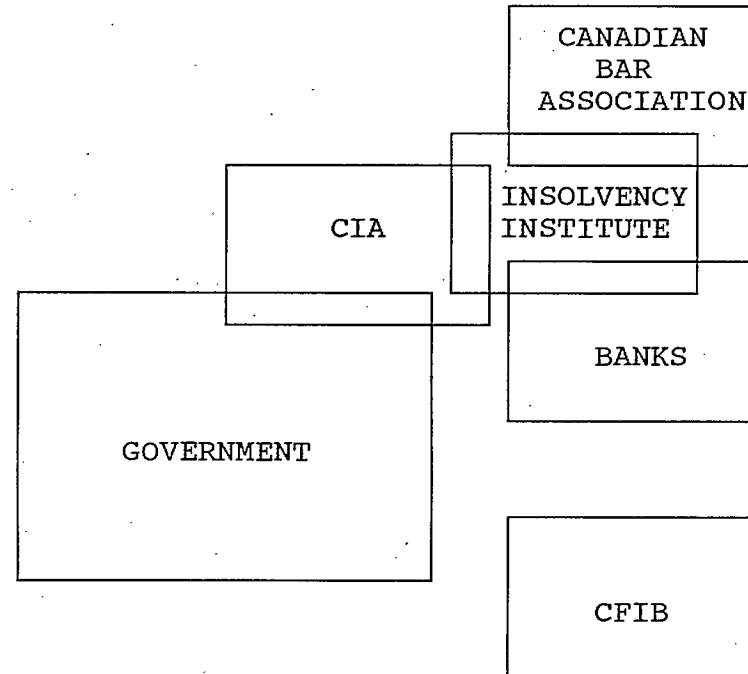
**Financial Executives** In their capacity as the managers of the unsecured trade credit market

# THE EVOLUTION OF INSOLVENCY PARTNERSHIPS

1988

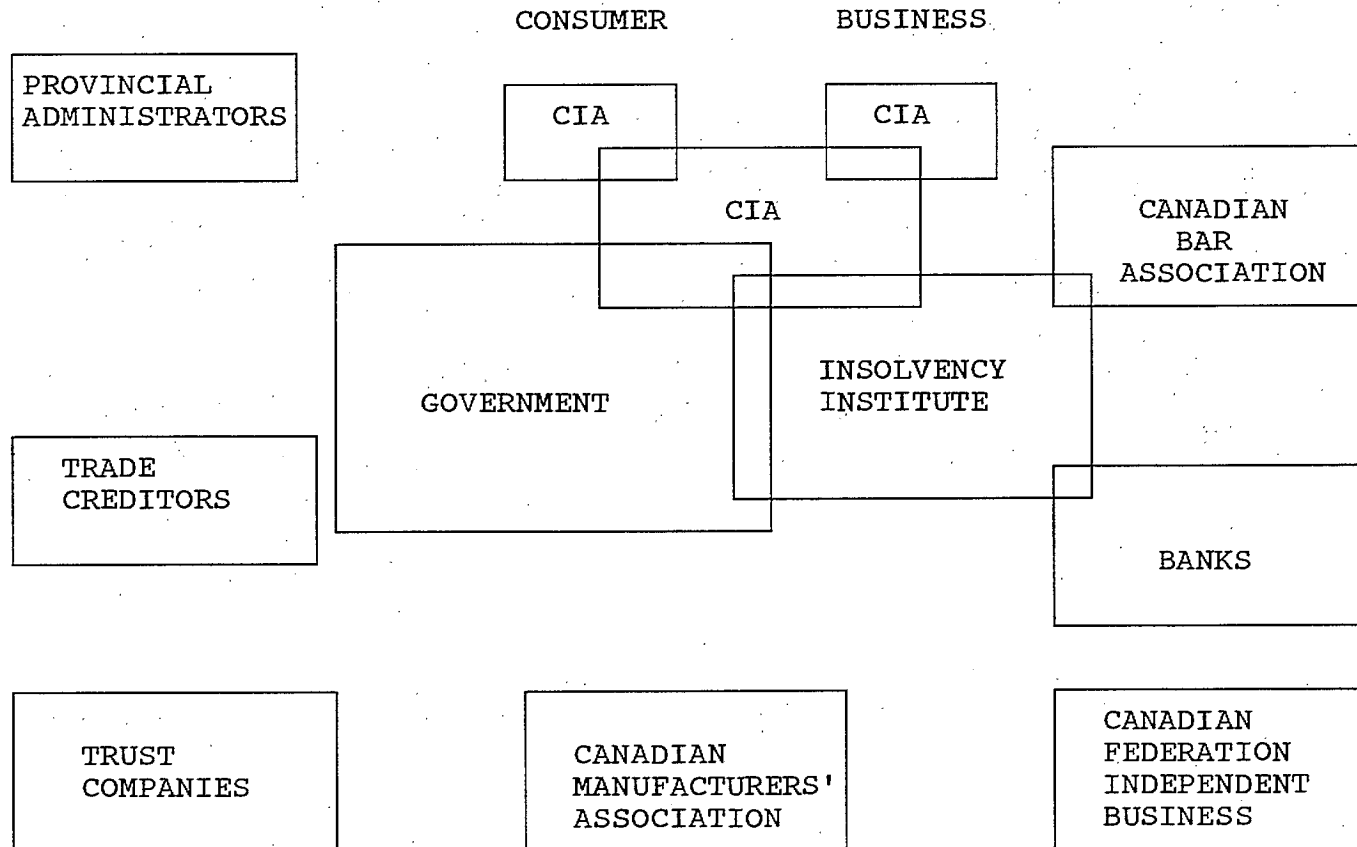


1990



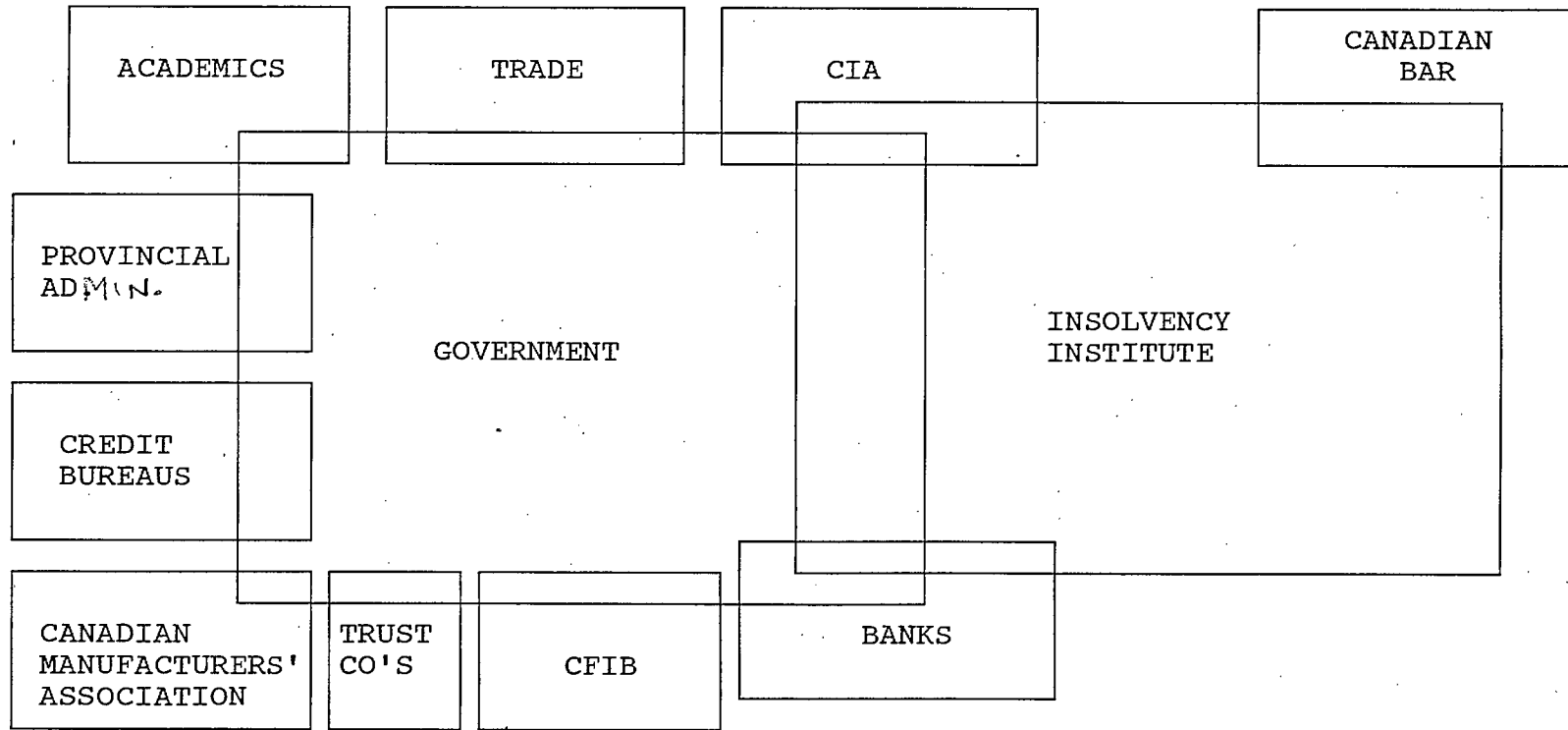
# THE EVOLUTION OF INSOLVENCY PARTNERSHIPS

1991



# THE EVOLUTION OF INSOLVENCY PARTNERSHIPS

1992





## Financial Sector partnerships

In his recent book "**The Competitive Advantage of Nation's**" Harvard Professor Michael Porter draws attention to the various national differences in private sector/government partnerships around the world.

The same point has been made in Canada by Sylvia Ostry (amongst others), who believe we need to examine the relationship between the risk capital providers in our economy and the business they seek to assist. In particular, to examine the way in which business, government and the financial sector can work together to share the costs of achieving competitive global success.

### **Government's and Corporations in a Shrinking World**

A major determinant of competitiveness is investment. Differences in the cost of capital among countries are very important in influencing investment performance. While many factors affect the cost of capital differences in capital, market structure also account for significant differences in capital cost among countries.

One key difference relates to the role of banks, which is much greater with respect to corporate financing in Japan and Germany than in North America and the United Kingdom. A Federal Reserve Bank of New York study points out the following:

"Close relations between corporations and banks in Japan and Germany and official efforts in these countries to reduce the private costs of corporate distress permit corporations to finance themselves in ways that cheapen the costs of funds. In particular, greater integration of industry and banking in Japan and Germany has permitted higher leveraging without raising bankruptcy rates much above those in the United States and Britain. The stronger ties between corporate borrowers and their banks also reduce the liquidity risk that a firm runs by borrowing so much at short term. Backstopping private creditors' management of difficulties is the Japanese and German governments' predictable willingness to spread the adjustment costs beyond the immediately involved workers, management, creditors and shareholders to business customers, consumers and taxpayers."

## The financial services industry - Managing failure and distress

The financial services industry has always had an interest in the nature of the insolvency regime. However, as the market has become more sophisticated and the volumes of both outstanding business and personal debt have grown, these institutions can rightfully claim to now have an even greater and growing stake. This includes not only an interest in the nature and application of insolvency legislation and in the general debate surrounding the management of both consumer and business financial distress as a whole, but it also includes a strong interest in the **prevention** of the problem in the first place.

The role for the financial institutions in this process has not yet been well defined. Indeed, it can be argued they are partly to blame for adopting too narrow of a "**special interest**" attitude. The fact remains, from the Governments standpoint, very little work has been done to quantify the way in which these institutions manage their loan risk portfolios relative to the bankruptcy process.

What we do know, is that financial failure and loss due to bankruptcy and insolvency is a natural part of lending activity. There is no known or possible way to totally avoid such losses even were it to be deemed a desirable social and economic goal which, in a free market economy, it is not.

In their recent brief to the Parliamentary Standing Committee, the Canadian Bankers Association made the point, in their view, there is a significant risk that changes to the insolvency legislation will not only affect the way in which financially distressed or bankrupt clients are managed by them but that such changes are also likely to have an impact on those who are financially sound and viable.



In other words they are claiming that, because the management of financial risk is not a pure science and lenders are conservative by nature, there are likely to be broad policy and lending practice changes which will be implemented by the financial community as a direct result of Bill C-22 and these will effect the entire market, not just the few who go bankrupt.

Unfortunately (and to the detriment of both sides in this debate) there has been no readily available or objective statistical evidence presented to either support or refute this contention. The gap in understanding on this point and the lack of solid data to support or test the thesis, places both sides at an unfortunate disadvantage.

This, in itself, should be sufficient motivation for both sides to work towards a broadening of the dialogue and a deepening of the partnership as it relates to insolvency law and practice. It is in the best interests of an efficient and competitive market, to include all forms of lending institutions in the consultation process and through that to develop a much deeper mutual appreciation of market realities and behaviour.

To this end , The University of Western Ontario recently published a study entitled "**Banks and the Small Business Borrower**". This study contains some very useful data on the market practice of the major Chartered Bank lenders as it affects their Small Business Clients.

A review of some of the more relevant facts exposed in that study would help serve as a useful base from which to build a better appreciation of the lenders perspective.

**Domestic loan losses of the Chartered banks  
1987 - 1989**

**Chart 1**

**Losses as a % of average loans**

| <u>1987</u> | <u>1988</u> | <u>1989</u> | <u>Average</u> |
|-------------|-------------|-------------|----------------|
| .59 %       | .23 %       | .35 %       | .39%           |

In this Chart, it will be seen that actual annual loans losses (in percentage terms) might be considered rather low - at less than one half of one percent (.39 %) of the total loan portfolio of the major Chartered banks.

However, in reality, the actual dollar value of losses is quite high given the size of the consolidated loan portfolio which will be outstanding at any one time.

The total loss provisions in 1990 were as follows:

|                       |                           |
|-----------------------|---------------------------|
| <b>Domestic banks</b> | <b>\$ 1,692.4 million</b> |
| <b>Foreign banks</b>  | <b>273.9 million</b>      |

In other words, total loss provisions from the banking sector only were over \$ 2 billion in 1990.

Another useful way to look at the loss experience numbers is to compare the loan loss provisions (as a percentage) to the Total interest Income earned by the banks.

Expressed in this way the losses range from:

**6.3 % to 1.2 % .....for the 8 Domestic Banks**

**and from**

**91.2 % to .3 % .....for the 39 foreign banks**

It will be obvious, that while the rate of loss fluctuates from year to year (and very dramatically from institution to institution in any given year) it has proven virtually impossible for the industry to manage the losses at anything approaching a static or core level.

This reality is sometimes confused with the impression that the banks are immune to certain level of loan loss and are prepared to accept it as a simple cost of doing business. In reality, the banks are relatively sophisticated in managing the portfolios and assessing risk but can not, despite all their systems and all of their expertise, ever hope to totally eliminate the losses.

## The Workout Factor

The more important factor to consider when evaluating the actions and attitudes of lenders with respect to financial distress and insolvency is, actually, the level of "non - performing" loans they carry on their books at any one time. That is to say, the portion of all loans which are not being properly serviced as to interest and/or principal.

The bankers will normally refer to these as "workout situations".

### Chart 2

#### Non-performing loans as a % of Year end loans

| <u>1987</u> | <u>1988</u> | <u>1989</u> | <u>Average</u> |
|-------------|-------------|-------------|----------------|
| 2.00 %      | 1.13 %      | .67 %       | 1.27 %         |

As Chart 2 indicates, there are two factors which are quite different from the picture initially painted in Chart 1.

1. The actual percentage on non-performing loans has been falling steadily since 1987 from 2.0 % to .67 % and
2. There are considerably more loans in the non-performing category than there are in the loss category

What does this mean?

In the first instance, whereas the banks cannot possibly manage the actual losses to the point of totalling eliminating them, they can manage the process by which they informally work with clients (outside of the bankruptcy and or insolvency process) to overcome the obstacles and place the borrower back on a sound footing without incurring a loss.

It would appear the banks, as a whole, have been doing a much better job of resolving financial conflicts in this way than ever before and this lends credence to the contention on their part that they are displaying a more constructive and tolerant attitude than in the past.

The final point we can make with respect to these figures has to do with a comparison of "loan losses" to those in the "non performing" category. This provides as good an estimate as is possible, to the extent of "financial distress", as opposed to bankruptcy.

**Comparison of Non-performing Loans  
to  
Actual Loan Losses**

|                | <u>1987</u> | <u>1988</u> | <u>1989</u> | <u>1990E</u> | <u>1991E</u> |
|----------------|-------------|-------------|-------------|--------------|--------------|
| Losses         | .59         | .23         | .35         | .42          | .49          |
| Non-performing | 2.00        | 1.13        | .67         | 1.57         | 1.65         |
| Ratio          | 3.38x       | 4.91x       | 1.91x       | 3.73x        | 3.36x        |

As we can see, while the extent of "non-performing" loans has been falling steadily, the ratio of "non-performing" to "losses" has been erratic, from a high of almost 5 times in 1988 to a low of 2 times in 1989.

The fact remains that due to better overall portfolio management and a more responsive attitude towards "workout", there are still far more loans being worked out informally than are subject to loss through bankruptcy.

## Total Factor Analysis

If we place this "workout" factor against the Business Bankruptcy numbers for the same years we note the following:

| <u>Year</u> | <u>Actual Bankruptcies</u> | <u>Workout Factor</u> | <u>Total Financial Distress</u> |
|-------------|----------------------------|-----------------------|---------------------------------|
| 1987        | 7,659                      | x 3.38                | 25,889                          |
| 1988        | 8,031                      | x 4.91                | 39,432                          |
| 1989        | 8,664                      | x 1.91                | 16,548                          |
| 1990(E)     | 11,642                     | x 3.73                | 43,424                          |
| 1991(E)     | 15,000                     | x 3.36                | 50,400                          |

This "total factor analysis" is a far more realistic gauge of the financial distress universe than the bankruptcy numbers alone. Regrettably, it is still far from scientific it provides and one further reason for actively involving the banks in the consultation process as we must come to better understand the magnitude of the universe impacted by the insolvency regime.

This may in fact, lead us to an acknowledgement that the "market" impacted by the legislation is, in fact, far greater than we understand and the bankers are correct when they become concerned about the impact of the legislation on their entire client base.

Another piece of evidence pointing to the need to examine the "**wider universe**" theory of insolvency is contained in various studies relating to the "**corporate life cycle**".

According to The Minister of State for Small Business (1989) who examined this issue between 1978 and 1987, there is a large number of businesses which can be expected to "**disappear**" each and every year. While not all of them fail through bankruptcy (and some are in fact merged with others), the fact of the matter remains:

#### **Corporate Life Cycle**

**53 % - of all business formed in 1978 had failed by 1987.**

**This ranged from 60% in the Business or Personal Services sector to 29% in community services**

**23 % - failed to survived the first year**

**28 % - failed to survive the second year**

**48 % - failed to survive until the third year**

In other words, not all businesses fail because of the withdrawal of credit by lenders. In fact, quite the contrary. The majority fail for a variety of other non-financial reasons.



According to the same UWO study we referred to earlier, their examination of 200 "sample failures" were as follows

Reasons for the Company's Failure in the Problem Loan Sample

| <u>Reason</u>                       | <u>%</u> |
|-------------------------------------|----------|
| Poor management skills:             |          |
| Financial                           | 46.0%    |
| Marketing                           | 35.1     |
| Operations                          | 34.2     |
| Inadequate equity capital           | 32.7     |
| Adverse developments in the economy | 14.9     |
| Personal problems of the principal  | 13.4     |
| Unrealistic plans and projections   | 8.0      |
| Difficulties with major suppliers   | 7.4      |
| Problems in collecting receivables  | 6.9      |
| Loss of key management              | 6.4      |
| Fraudulent business activities      | 3.0      |
| Excessive cash drains by owner      | 2.5      |

\* Adds to more than 100% because of multiple responses.

## **Lenders and their Security**

There is a final misconception about lending practice and the behaviour of lenders in situations surrounded by financial distress. This relates to the nature and extent of the security which a bank may take to protect its risk position. It is often charged that banks overly protect their position and move to obtain extra security when financial failure is imminent.

The facts would seem to be otherwise. Indeed, while Inventory and Receivables are indeed the most common type of security taken for business loans (and, in fact, may be taken in tandem) security of this type is taken in less than half the cases.

The major categories of security taken by banks and their frequency is as follows:

| <u>Type of asset</u> | <u>Percentage of cases</u> |
|----------------------|----------------------------|
| Receivables          | 55.9 %                     |
| Equipment            | 30.3 %                     |
| Inventory            | 28.9 %                     |
| Vehicles             | 12.3 %                     |
| Land/buildings       | 9.0 %                      |

In the case of realisations upon that security, it has been shown that recovery is significantly less than 100 cents on the dollar.

In fact, it amounts to only 66 cents on the total value of all security taken.

In terms of recovery (by category of security) it is:

60 % .....on Guarantees

87 % .....on machinery

71 % .....on receivables

41 % .....on inventory

These are the type of historical recovery rates that the banks use in "**margin**ing" their security and are the rates which they feel may be subject to further deterioration as a result of the 30 days goods, super priority and other changes contained in Bill C-22.



## The nature of the consultation process

We have now had the opportunity to examine each of the major factors which influence the insolvency system and those which are currently forcing us to re-examine our role and the way in which we wish to conduct it.

The challenge is to set a new **"vision"** based upon consultation and partnership with the private sector and to this end;

### We have:

- examined the nature of the rising level of bankruptcies and the likelihood they will plateau at a new and higher **"core"** level than ever before

### We have:

- established that the bankruptcy numbers do not, in themselves reveal the true extent of financial failure and in fact reveal only a small fraction of the overall level of financial distress, being experienced at both the consumer and business levels

### We have:

- recognized the emergence of professionals outside of the Trustee community who have an active interest in the insolvency field

### We have:

- acknowledged the broad **"macro"** economic environment we are likely to continue to face as the economy restructures itself to compete globally

### We have:

- accepted the restraints under which the Public Service will operate and the initiatives under way for implementing a new management style and philosophy

**We have:**

- assessed how the financial services industry has changed and is likely to develop in the future

**We have:**

- demonstrated the emergence of new players in that sector and the important role of the Trade Creditor  
and finally;

**We have:**

- been forced to accept the need to reevaluate our management process and priorities and to find new ways to do more while better serving our constituents and more closely involving them in the process

The "**vision**" or "**mission**" we set must be built upon the twin commitment to "**consultation and partnership**".

The "**vision**" must recognize a new role for Government and a fundamental shift in both culture and attitude. The process must be set against the backdrop of wider responsibility and accountability and established upon an entirely new and progressive footing.

We must begin the process by establishing a new "**paradigm**", clearly setting out and communicating the principles by which we will open up the "**partnership and consultation**" process. We must seek to combine the most relevant of widely accepted modern business management techniques and balance them against the unique requirements and demands of effective Public Service.

This will not be an easy task. The process of change will take an unusually high level of senior management commitment and time. Risks will have to be taken. Mistakes will be made.

The process is nothing short of an **"investment"** which will only **"pay off"** over time depending on the amount of capital invested at the outset.

The process of consultation must abide by certain rules and these must become the **"Guiding Principles"** governing the initiative.

### **The Ten Rules for Effective Consultation**

1. The role of the Government should be as a "facilitator"
2. The "engine" should be private sector dominated
3. The process must place emphasis on "private sector responsibility" and the ultimate goal of self regulation of the insolvency process
4. The "consultative net" should be cast as wide as possible
5. Priority must be placed on the "educational and research and development" aspects of the insolvency process
6. The emphasis must be on "building bridges" and forming new linkages
7. The process should be rigid in structure and yet "fluid and flexible" in format
8. There should be a maximum amount of "field/regional involvement"
9. Goals/targets must be set and the results "regularly measured"
10. Everything about the process should represent the highest standard of "quality and professionalism" possible

## **Setting the wheels in motion**

The process of effective consultation and the formation of meaningful partnerships must have both short and long term objectives.

These objectives should be both **"quantitative and qualitative"**.

The initial focus should be kept simple and **directed towards;**

- **Education**
- **Research and development and**
- **Networking**

The short term **"objectives"** should be to:

- **Monitor the market impact of Bill C-22**
  - **Begin the process of debate, re-evaluation and assessment**
- and**
- **Establish the means for reaching a consensus on modifications, changes and enhancements for the Parliamentary Review in 3 years time**



The ultimate, "long term", goal should be:

- to place the insolvency process firmly within the wider context of financial distress
- to achieve a significant reduction in the long term trend and core number of bankruptcies
- to establish a program for the effective prevention of financial distress and
- to establish the means for greater self regulation by the professional insolvency bodies

## THE OBJECTIVES MATRIX

### QUALITATIVE GOALS

### QUANTATIVE GOALS

Short Term  
Goals

- Research & development
- Networking
- Education

- Broaden the debate
- C-22 Monitoring
- Committee work

Long Term  
Goals

- Alliances of understanding
- Consensus
- Privatization

- Reduce bankruptcies
- Prevention
- Self regulation

## Changing the "paradigm" ...

At the present time, the formal insolvency world revolves around the power of the Superintendent of Bankruptcy and his ability to issue licenses and initiate disciplinary proceedings. The market's view of the process is in keeping with their traditional view of the Government as the "**regulator of a bureaucratic process**".

As we know, there are pressures demanding a reassessment of this role and a total re evaluation of the government-private sector relationship.

In this climate, the "**litmus**" test will ultimately be in terms of our efficiency and relevance to the insolvency process.

**Efficiency ....** in terms of how well we perform and how well we serve all of the constituents and

**Relevance ....** in terms of whether or not we can carve out a justifiable, meaningful and value added new role for ourselves, within the changing market context and against the demands and constraints under which the Public Service will be operating

This requires nothing less than a dramatic "**repositioning**" of the Superintendent's role to ensure these two qualifications can, in fact, be successfully met.

At the very heart of this "**repositioning**" is an acceptance of the need for a new "**paradigm**" based upon a strong commitment to the twin concepts of consultation and partnership.

A commitment that places the Superintendent in a broader and more influential context than ever before. One which ensures the Department:

- becomes "market driven"
- "client focused" and
- "interactive" with the private sector

This "**vision**" would have the Superintendent act as not only the "**custodian**" of the insolvency process but also as the "**facilitator**" for consultation with the private sector constituents and other Government Departments, both federally and provincially.

It would place a far greater burden on the Superintendent to interact with the entire market (not just the Trustee Community) and to be responsible for the formulation of the long term strategic plans and programs necessary to achieve the national objectives.

This dramatic change in approach is necessary in order to fully recognize and address the emerging reality of the professional insolvency process.

It is necessary in order to:

**Recognize that:**

1. The insolvency process needs to be more effectively linked to the whole economic revitalisation agenda and can no longer operate in isolation

**Acknowledge that:**

2. The insolvency process is much wider than is reflected in the bankruptcy numbers alone

**Accepts that:**

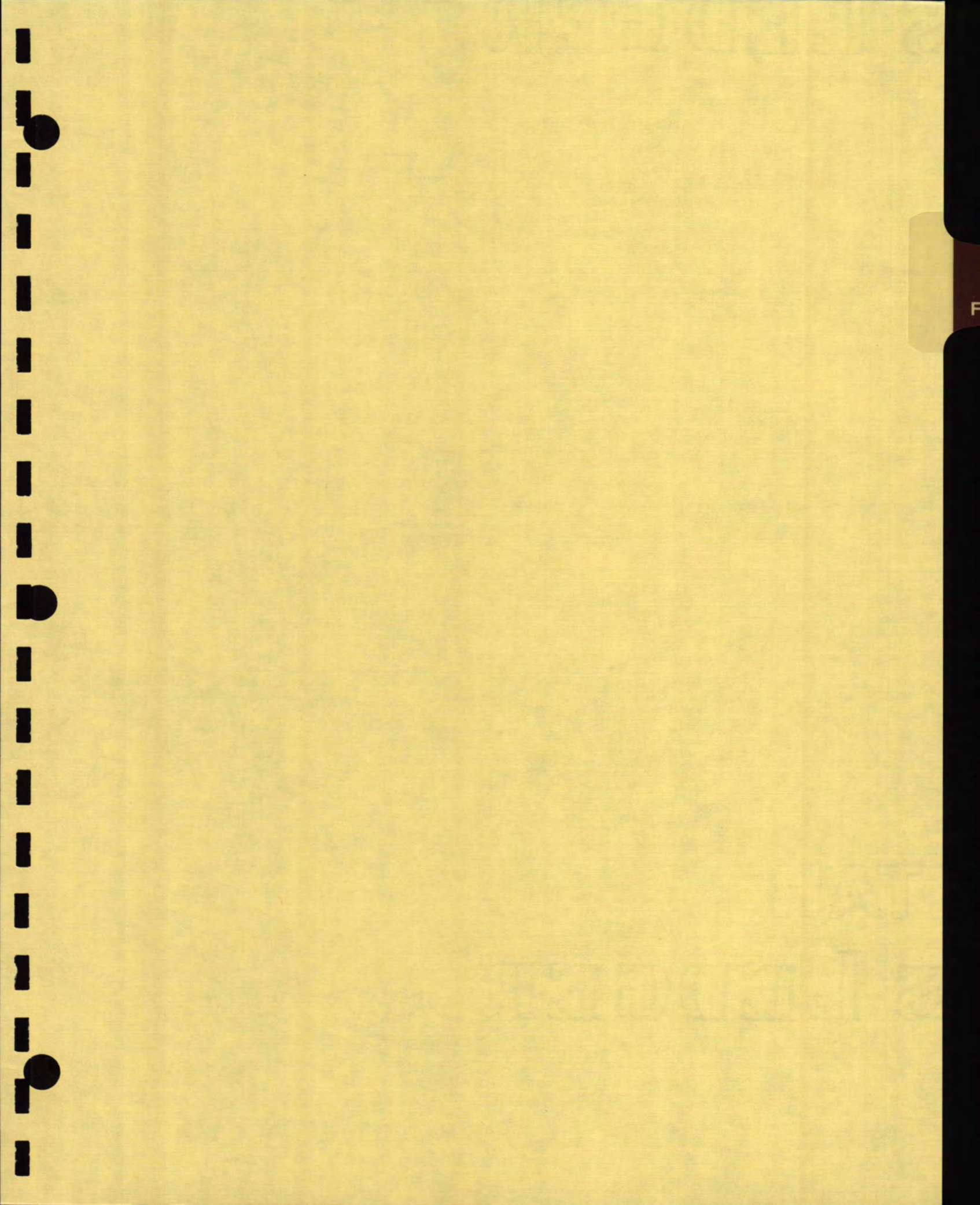
3. The Department has a responsibility for the integrity of the system that goes beyond the licensing of Trustees and the processing a bankruptcy files

**Believes in:**

4. The need to interact with all of the constituents in the system, including the lending community and finally

**Commits to:**

5. The responsibility for not only administering the fatalities of the insolvency system but also seeks to find an answer to their prevention.



## Implementing the action Plan

Any effective "**business plan**" will contain several elements which must be moulded together and forged into a effective package. Often, the final objective may seem elusive at the beginning and will only come into sharper focus once the process has begun. It is also fair to say that in any "**bold plan**" you have to be prepared to take risks. That means setting the objectives high enough that they create an energy of their own and a "**vision**" that can be accepted by a broad range of players.

This will certainly be the case with any plan to reposition the Superintendent and establish a lasting commitment to consultation and partnership.

As we have noted earlier, there are two "**elements**" which need to be put in place before we can build the plan:

**The first ..... is a rationale for the process and**

**The second ...are the objectives themselves**

We have already provided a conceptual framework for these criteria in our "**Objectives Matrix**" and they now need to be explained in somewhat more detail.

## **Rationale for the consultation process**

Simply put, the rationale for a programme of consultation with the private sector is to place the Superintendent in a new "**leadership role**" within the insolvency world in the areas of:

**Education**

**Research and development and**

**Networking**

This is to say, placing the Superintendent in an entirely new light within the insolvency community at large in such a way as he becomes the "**facilitating focal point**" for the establishment of a multiple set of cross disciplinary professional partnerships.

The consultation process must be "**sold**" to the private sector on the basis of merit and must permit all parties to view the three priorities as a common objective.

This will only be possible if we ourselves have a clear belief in the rationale for each priority.

A more complete explanation now follows.



## **Priority 1 ..... Education**

There is an increasing acceptance in society today that we all need to do more in support of education and towards improving the knowledge and competence levels of the community. In the context of the insolvency universe (as we have now redefined it), there are several issues we can probably all agree upon including the belief that:

- **We can all learn something about the insolvency process from the other professional constituents**
- **No one constituency has all the answers or all the necessary knowledge and**
- **The more we know collectively, the better off the system will be overall**

Consistent with the overall thrust of the consultation process the objective (in the education area) should be on the formation of:

### **"Alliances of understanding"**

This will take the form of a complex **"web"** of communications and information sharing wherein the Superintendent will act as facilitator, score keeper and referee.

It recognizes the need for an upgrading in knowledge between:

- The Superintendent and..... the financial community**
- The trustee community and..... the financial world**
- The trade and business groups and... the Superintendent**
- The academic community and..... the insolvency professionals**

## Priority 2 .....Research and development

In today's world, there are constant demands on all of us to keep one eye focused on the future and not become so comfortable with the present that we fail to adapt to the changes going on around us.

It is entirely consistent with this reality that the Superintendent should reposition himself in a leadership role in the area of Research and Development in the field of insolvency. Ensuring there is always a healthy and vital degree of work being done in this field from a developmental perspective.

This must, once again, be a role in which the Superintendent seeks not to be at the centre of the knowledge base himself but rather cajoles and sustains an effort on the part of the private sector constituents.

It also acknowledges that any future amendments to the insolvency regime deserve to be evaluated in the light of accurate and thorough empirical data of a kind we simply do not presently possess.

Finally, it is based upon a premise that suggests (in the spirit of creating breakthrough opportunities for Canada) that we might actually wish to rethink the insolvency process from the ground up, rather than simply modifying and amending as we go.

A emphasis on the need for ongoing Research and Development in the insolvency arena would recognise:

**The insufficiency of our current demographic data and statistical analysis on bankruptcy**

**The incomplete nature of our "universe" of information on the much wider field of financial distress**

**A lack of understanding as to the practical application and possible results of the implications of Bill C-22**

**The needs and benefits of placing the whole subject of insolvency under an experimental or scientific light**

**The wisdom and desirability of creating an awareness of international developments in the insolvency field**

### **Priority 3 .....Networking**

At the very centre of the consultation initiative is a belief in the desirability of creating a truly "**dynamic**" environment in which the various constituents interact with and learn from each other. In the process, they will create a momentum and common vision which benefits the system as a whole.

This network of "**partnerships**" can not simply be constructed at the centre but must spread out to the field and thereby allow for regional issues to be dealt with locally. It must be a multi layer, multi dimensional initiative that permits all levels of the professional community to participate and creates a mechanism for both the identification and the resolution of problems and issues at the point closest to the source.... not from on high or from the centre.

Consequently, the networking element of the plan must support a system whereby "**bridges**" are built between:

**The national representatives of each constituency**

**The Superintendent and the national representatives**

**The Superintendent and the Regional Assistant Superintendents**

**The Regional Assistant Superintendents the Regional Constituents**

## Establishing Broad Objectives

Having now established a basis and rationale for entering into the consultation process, we must ensure the "**objectives**" are clear and are seen as worthwhile by all of the constituents.

They must be set in such a way that they are reasonable and provide for ready "**buy-in**" by the various parties. This means they must be linked to some form of self interest on the part of each group.

Bill C-22 essentially provides this impetus given the fact the legislation requires review, by Parliament, within three years. It is also provided in public statements by the Government indicating their commitment to an ongoing process and change and modernisation to the insolvency regime.

Even in the absence of these "**internal**" motivating factors, the fact remains that developments in the world at large are likely to force the country to be in a of constant state of examination of all of its framework laws and require us to regularly monitor their effectiveness in the global arena.

The message that should be sent by the Superintendent (with respect to this process) should be clear and visionary. It should emphasize the need for ongoing involvement by the private sector in the re-evaluation process. The immediate objectives should be framed in the context that:

**The amendment process must never again fall victim to the type of delays and bickering we have seen in the past**

**Future amendments must be made with a much better and more objective understanding of their impact and risks**

**The actual results of C-22 must be followed closely, specifically as it relates to (as an example):**

- credit availability and the 30 days goods provision
- the effectiveness of the counselling process
- the success in creating more proposals
- the receivership activities

All of this will, in turn, form the basis for a constructive and rational process of ongoing consultation leading to:

**The continuous evaluation of Bill C-22**

**The gradual emergence of a consensus on possible areas for change and improvement and**

**An clarification on future direction.**



## **Implementing the consultation process**

If the consultation process is to succeed and achieve any of the objectives we have outlined so far, there will be at least five critical issues which will need to be addressed at the outset.

These will include:

- 1. Gaining the initial co-operation and support**
- 2. Projecting the new mandate**
- 3. Securing sincere ongoing commitment**
- 4. Establishing the proper framework and**
- 5. Ensuring full and diversified involvement**

In his role as "facilitator" it is important the Superintendent not attempt to directly structure the consultation framework. This must come from the constituents themselves and over time, they should determine the precise nature of the forum they think is best likely to produce the desired results.

The Government's initial role must be restricted to:

- **establishing the initial Forum**
- **energizing the Mission Statement and**
- **ensuring the ongoing commitment of all parties**



This will be a new role for the Department and is an attempt to position the Government as the "**conscience**" of the insolvency system and not just the regulator of the bankruptcy process.. As we have seen earlier, the role should be to set the vision and then cajole the constituents into committing their time, resources, energy and intellectual talent.

While the process should not be managed at the centre (by the Government), there are several components that can be orchestrated by the Superintendent.

This amounts to the creation of a "**Blueprint for action**" and it includes several very precise and discreet steps.

## Phase 1 - Establishing the new "mandate"

The process of "**repositioning**" the Superintendent should begin by establishing a "**master plan**" in a way which creates a sharp distinction, in the eyes of everyone, between the ways of the past and the route to the future.

This division must be in terms of both "**substance and style**".

The initial approach should be built around ways in which to "**shock the system**" and thereby gain both the attention and the curiosity of all of the various constituents.

The first step would be to:

**Step 1.** Assemble a master "**contact list**" of key professionals from each of the constituents. This would include:

- all Trustees
- all insolvency lawyers
- the Chief lending officers of each financial institution
- the large trade creditor groups
- the Executive Directors of each business group or Association:
  - Canadian Bankers' Association
  - Canadian Federation of Independent Business
  - Canadian Manufacturers' Association
- key academics

**Step 2.** A personal letter should then be sent (by the Superintendent) to each of the key contacts announcing his intention to establish a formal private sector/government consultation process and linking it into the:

- the **Government's PS 2000 Program**
- the **"Prosperity Initiative"** and
- as part of the **Phase 2 preparatory work**

The letter would state the basic objectives and rationale for the implementation of the process and would place it in the context of the enactment of the new Bill and the opportunity which its passage creates for the establishment a new **"partnership of consultation"** in the future.

The letter would advise the constituents of the Superintendent's intention to make cross country tour to speak to regional groups.

**Step 3.** A series of public speeches would be lined up for the Superintendent in each major city across the country (all to be conducted within a one week window).

This **"road show"** would stress the importance of the new initiative and would represent a clear and direct appeal for the insolvency community to come together and commit to the process.

The tone would be one of challenging the private sector to rise to the occasion and volunteer their efforts.

## Phase 2 - Projecting Sincere Ongoing Commitment

Following the despatch of the letter (Step 2) and the cross country speaking tour (Step 3) the plan should be to quickly establish a new means of communicating with the constituents in a way which projects sincere ongoing commitment.

This can be done in several ways and the steps should include;

**Step 4.** Redesigning the **Superintendent's Monthly Bulletin** and expanding its readership on a self financing "**subscription**" basis. The first issue of the reformatted publication would be to recap the message sent out in the letter and carried in the "**road show**".

The format should be modified and its message broadened to cover the wider spectrum of financial distress. A guest Editorial board should be formed of private sector government officials and the publication would be positioned as "**the definitive authority**" on insolvency and financial distress in Canada.

**Step 5.** Following the conclusion of the "road show" individual meetings or contract negotiations should be held with the Executive Counsel or Board of each of the key constituent groups. These should include (but not necessarily be limited to)

- **The Canadian Insolvency Association**
- **The Insolvency Institute**
- **The Canadian Bar - Insolvency Branch**
- **Canadian Bankers' Association**
- **The Trust Companies Association of Canada**
- **Canadian Federation of Independent Business**
- **Canadian Institute of Financial Executives**

The meetings would be arranged with the objective of "**personalising**" the message and making it clear that we are looking for private sector partnerships and that we will be restricting our role to acting as the moderator or facilitator. They must realise they are being asked to rise to the occasion and "**carry the freight**".

### Phase 3            **Gaining Initial Co-operation and Support**

The "**contract negotiations**" would be set up with the very specific intention of obtaining the private commitment of each group to the process of consultation.

The meetings should be straight forward, blunt and business like. Consequently, there should clear expectations established at the outset.

These steps would be as follows:

**Step 6.** Prior to the meeting, each group would be informed we will be specifically asking them for the following:

- (i)        The name of a "**consultation**" team leader and an alternate
  
- (ii)       Their commitment to attend a two day **National Conference of Insolvency Constituents** and
  
- (iii)      A clear statement of the 3 key issues and/or priorities of their group

Step 7. The groups should also be left with a very clear statement of our expectations of them.

This may be the most difficult message to convey and it will naturally have to be personalised to the specific group. This will form the basis for what we will call the "**consultation contract**".

These "**contracts**" will have to be developed but they would be something like this.

|                  |                                                                 |
|------------------|-----------------------------------------------------------------|
| Canadian Bankers | A commitment to share their information on non performing loans |
| CFIB             | A commitment to provide data on new business formation etc      |
| Credit cards     | Delinquency and loss reports                                    |

## Phase 4 Ensuring Full and Diversified Involvement

It would appear as though one of the most significant roadblocks to amending the insolvency process in the past has been strong "**special interest**" posture of each constituency and the fact all previous debates have centred on the realignment of legal rights.

This atmosphere and approach must be changed (or at least tempered) through the development of:

- a better, mutual understanding of the basic role of the insolvency process
- its ultimate legal and social objectives and
- its place within the economic restructuring process.

Admittedly this will not be an easy task!

One way in which to ensure this does, in fact, happen and yet also ensures the process remains properly balanced, would be to widen the consultative net and thereby to make it quite apparent to any special interest group that they are better off working from within the system.... rather than sniping at it from outside.

In effect, our challenge is to make each and every constituency feel that the "**consultative network**" is at the very heart of the process so that they not only want to be part of the network, but also feel there is some prestige or merit to being included.

As a result, we need to create what is in effect an elaborate series of "**checks and balances**".



For instance:

- **CFIB can not be allowed to become the sole voice for small business**
- **the CBA can not become a short cut means of communicating with each of the major banks**
- **the CIA can not be the only vehicle through which to talk to insolvency professionals**

In other words, we must attempt to find a way to transcend the "lobbyist" posture of the key groups and force cross professional consensus.

To do so we must establish the "**right to consult**". As in any service industry, the priority should be placed on:

- **quality service to the client**
- **putting the client first ... and**
- **being intimately involved with the client on a regular basis.**

This requires a significant commitment to regular visits with each of the key client groups and such monitoring techniques as client surveys etc.

The process must be one where the results can be measured and the progress against "**productivity**" and service targets monitored on a regular basis.

**Step 8.** We should begin by establishing a "**Client Contact Directory**" and assigning direct client responsibility for each contact to a specific senior member of either the Head office or Regional management team.

These lists should be treated as though they were individual "**client portfolios**" and it must be made clear to the "**Relationship managers**" that they will be assessed and monitored against their ability to service the client.

In effect (and in reality) client service and interaction with the constituents will become Priority Number 1.

**Step 9.** The list should include members of each constituency beyond those represented on the executive committee of the respective professional association.

In other words it should include:

- the senior lending officer of each major Bank, Trust Company, Finance Company
- senior management of every other major creditor community
- the management of the Credit Bureaus etc.

**Step 10.** Each member of the management team will be expected to enter into a "**Performance contract**" with the Superintendent whereby specific targets and goals are set for each "**portfolio**" in terms of:

**Quantitative expectations (the number and frequency of visits etc.)**

and

**Qualitative expectations (client specific goals)**

These will become the Key Result Expectations (KRE's) of each management officer.

**Step 11.** Each management officer will begin his or her visitation program and will meet with the Superintendent monthly to review the results against the plan.

## **Phase 5 - Establishing the Proper Framework**

As we have seen, there will be several levels of contact created with the private sector. These will include:

- 1. Individual client contact as well as**
- 2. Association contact**

A means of bringing the two together, i.e. some form of:

- 3. An Assembly of Associations**

Out of this Assembly will, in turn, come a series of:

- 4. Joint Committees (described more fully below) and**

Finally, the final level of interface will take the form of:

- 5. An Annual Conference of Insolvency Professionals.**

We have already dealt with the first two of these. Let us now examine the final three in greater detail.

## Step 12. - The Assembly of Associations

As we noted at the outset, the professional insolvency world has developed to the point where there are now three separate groups of insolvency professionals each of whom can claim their own "raison d'être".

The CIA

The Insolvency Institute and

The Canadian Bar

It should be stated quite clearly that our objective is not to interfere or replace the role of these Associations. Rather, our role is to facilitate an interaction amongst them and with the various other "stakeholder groups" who are not represented in these fora.

One such way would be through "An Assembly of Associations" for which the Superintendent would act as Chairman and moderator.

The first meeting of this group would be the most important.

It should be kept to no more than 20 people, with no more than two representatives from each constituency. The focus would be on networking and establishing a more formal means of sharing information and views. The importance of education as well as research and development would be stressed.

The structure of the meeting might be as follows:

**Day 1**

- 1. Brief presentations by each constituency**
- 2. An overview of the consultation process**
- 3. A Presentation on PS 2000**
- 4. A presentation by The Monitor Company or some other management consulting group or group on the challenges facing Canada in the 21st century**
- 5. Presentations by a leading expert on personal financial planning or management**
- 6. A presentation by a leading US insolvency expert**

**Day 2**

- 1. Individual workshops (discussion groups) on each of the following priority areas:**
  - 1. Consumer bankruptcy**
  - 2. Small business**
  - 3. Workouts and distress**
  - 4. International issues**
  - 5. Education**
  - 6. Research and development**

The balance of the second day would be spent in General Assembly, developing an action or implementation plan.

This would have several objectives in mind:

**DAY 2 (cont'd)**

1. The election of a "spokesperson" or Committee Chair for each of the six priority areas listed above
2. The formation of those six individuals and the Superintendent into a "Managing Directorate"
3. Obtaining the agreement of those spokespeople to:
  - the formation of a "Standing Committee" on each area to act as an advisory council to the Government
  - "quarterly meetings" of the Directorate

The objective would be to have each committee include a "cross section" of representation from each constituency, thereby forming an elaborate network of alliances.
4. Each Committee would then be asked to prepare a report on their topic for presentation at the Annual Conference. The report would be a "Strategic Plan" for addressing each priority to be placed before the Conference.

The key here would not be to necessarily elect an equal number of representatives of each and every constituency for each and every committee, but rather to make the Committees "topic specific" and cross disciplinary.

It should also be made clear at this point that the existing JCB would remain in existence as the advisory mechanism to the superintendent on matters directly affecting the Trustee community.

### Step 13. The Annual Conference

We have already accepted:

- a need for the dialogue to be as wide open as possible
- for the partnerships to be as diversified as necessary
- that there will be multiple levels of interest in the insolvency debate and process and for
- the right for each constituency to be heard.

Finally, we have set ourselves the role as "facilitator".

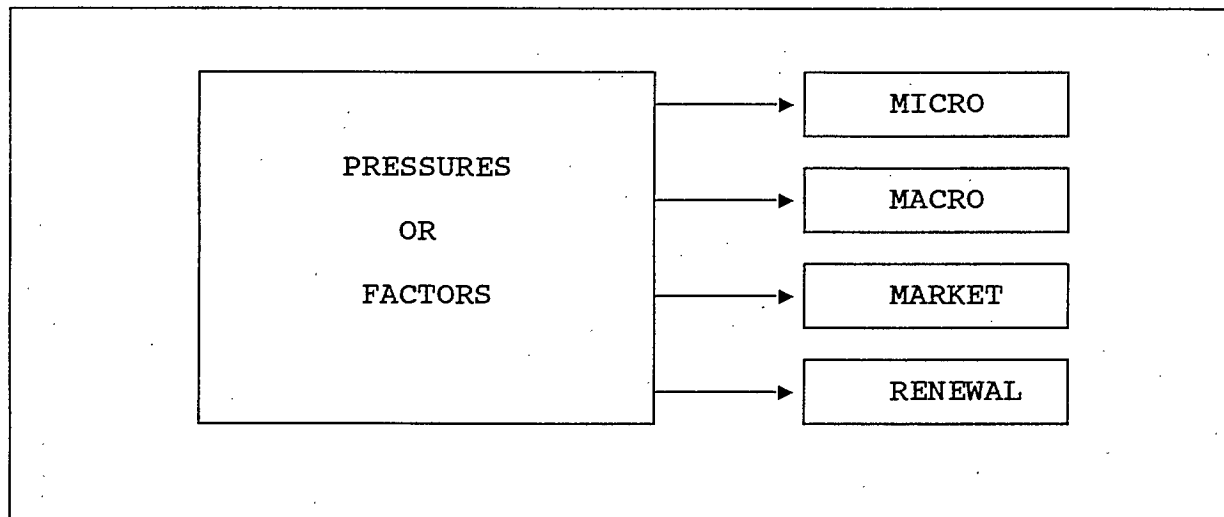
In this circumstance, it seems appropriate to have the Superintendent formally and publicly commit to an "**Annual Conference**" of the insolvency world (a State of the Union presentation or Annual Report).

This would be undertaken in the context of the Superintendent's responsibility (as custodian of the insolvency system) to make a public accounting or report on the insolvency profession and system as a whole.

In a manner of speaking, this would be a "mini" Auditor General's Report touching on the various aspects of the previous years activity and at which each of the Committee Spokespersons would be asked to present the results of their work.

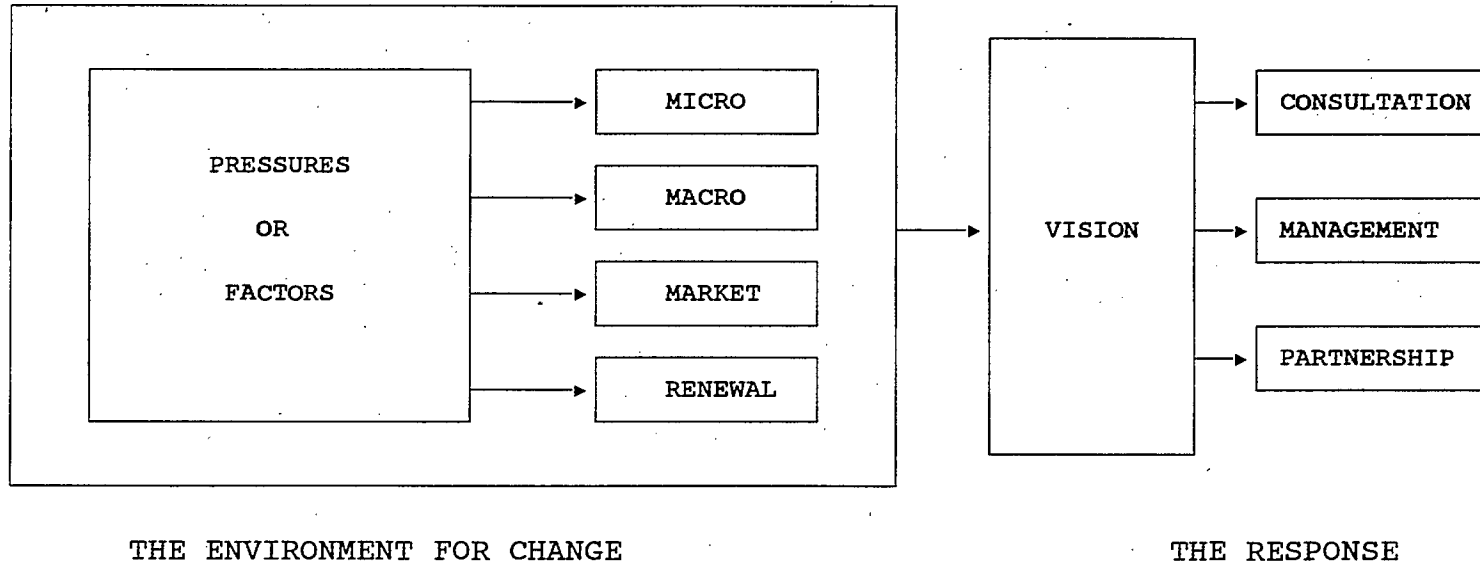


## DEVELOPING A PROCESS FOR EFFECTIVE CONSULTATION

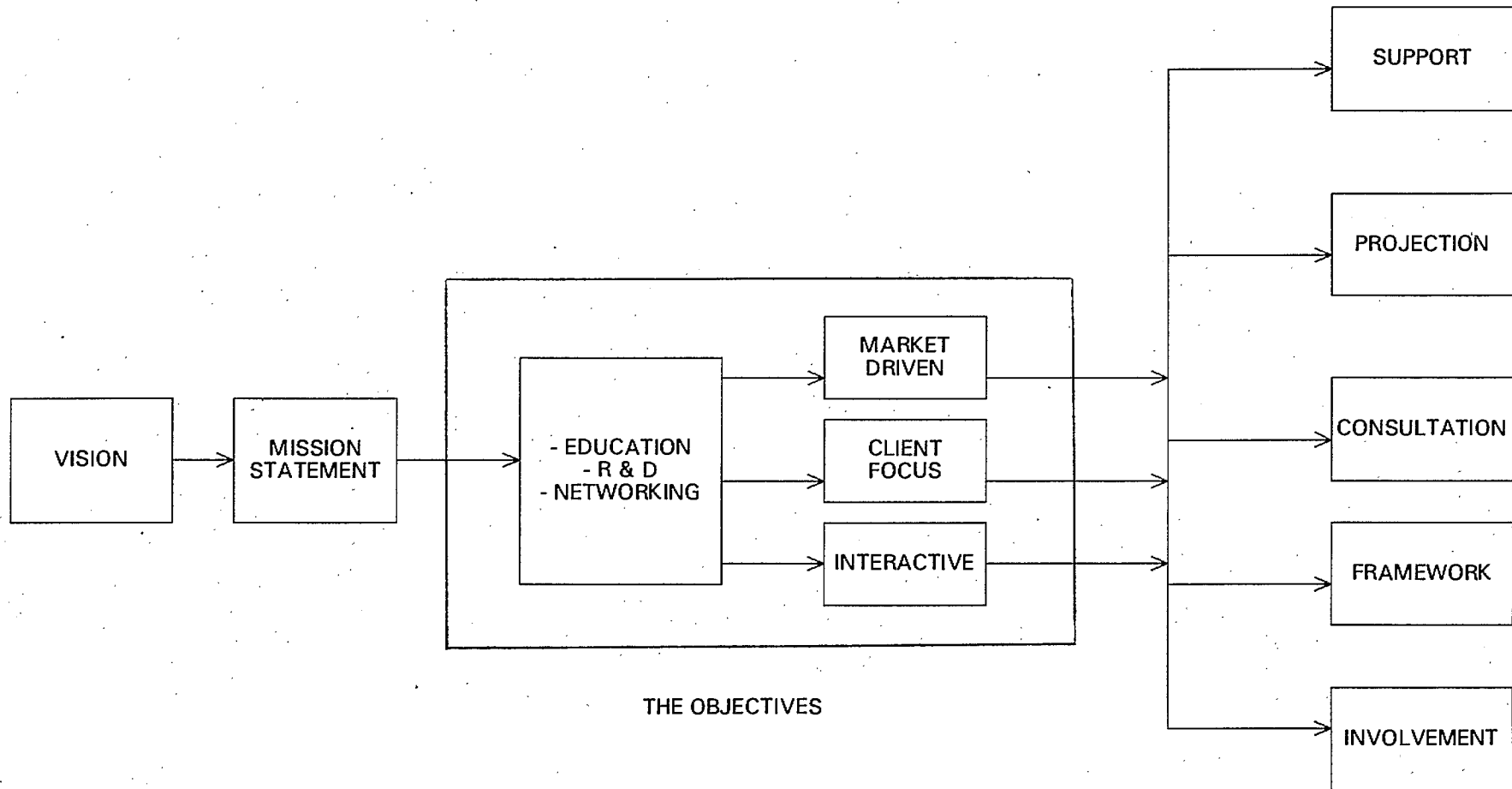


THE ENVIRONMENT FOR CHANGE

## DEVELOPING A PROCESS FOR EFFECTIVE CONSULTATION



## DEVELOPING A PROCESS FOR EFFECTIVE CONSULTATION



# DEVELOPING A PROCESS FOR EFFECTIVE CONSULTATION

## STEPS

### PHASE 1

SUPPORT

1. CONTACT LIST
2. PERSONAL LETTER
3. ROAD SHOW

### PHASE 2

PROJECTION

4. REDESIGN BULLETIN
5. CONTRACT NEGOTIATIONS

### PHASE 3

CONSULTATION

6. MEETING
7. CONSULTATION CONTRACTS

### PHASE 4

FRAMEWORK

8. CLIENT DIRECTORY
9. PERFORMANCE CONTRACTS
10. VISITATIONS

### PHASE 5

INSOLVENCY

11. ASSEMBLY
12. COMMITTEES
13. ANNUAL CONFERENCE



### **The next generation of changes:**

We noted earlier in this Report, our ultimate objective is not to make the Government the centre of this process from either an implementation or execution standpoint.

The objective is to:

- find a means of implementing private sector solutions
- establishing ongoing private sector initiatives and
- developing greater responsibility on the part of the professional insolvency community

The "**Blueprint**" we have outlined herein is intended to help achieve that goal but it is not an end in itself. In fact, it will only bring us to the beginning of what will be the most important part of the entire process.

**"The creation of a dynamic, self sustaining and self propelled initiative - fuelled by the desire and energy of the private sector to share responsibility with the Government and a willingness on the part of all parties to hold themselves accountable to the public at large"**

The simple fact of the matter is Government can not and should not attempt to drive the process.

Our role must be:

**To act as the "Chairman of the Board".**

**To set the "vision".**

**To foster the long term view.**

**To create a climate for change and dialogue.**

**To establish the vital partnerships.**

Each of these roles requires great skill and a redefinition of the way in which Government has traditionally sought to position itself in a regulatory process such as insolvency. It will not be easy!

## Conclusion

We have attempted, in this Report, to provide a fresh, all encompassing view of the unique possibilities which currently exist for us to create a "**quantum shift**" in the way in which the professional insolvency process is managed by Government.

We have sought to explain the many pressures which are being applied to the system today and those which are likely to apply in the future.

Our objective has been to stand back from the process and take the widest possible view of the "**challenge**", without surrendering to traditional methods or solutions.

We recognize the radical departure this Report suggests.

We make no apologies for it's philosophy or basic premise.

There are no easy answers to altering attitudes or breaking old habits. The goal, at every level of Canadian society today, should be to ensure the country is adequately equipped to compete effectively in the global market while sustaining a rising standard of living at home.

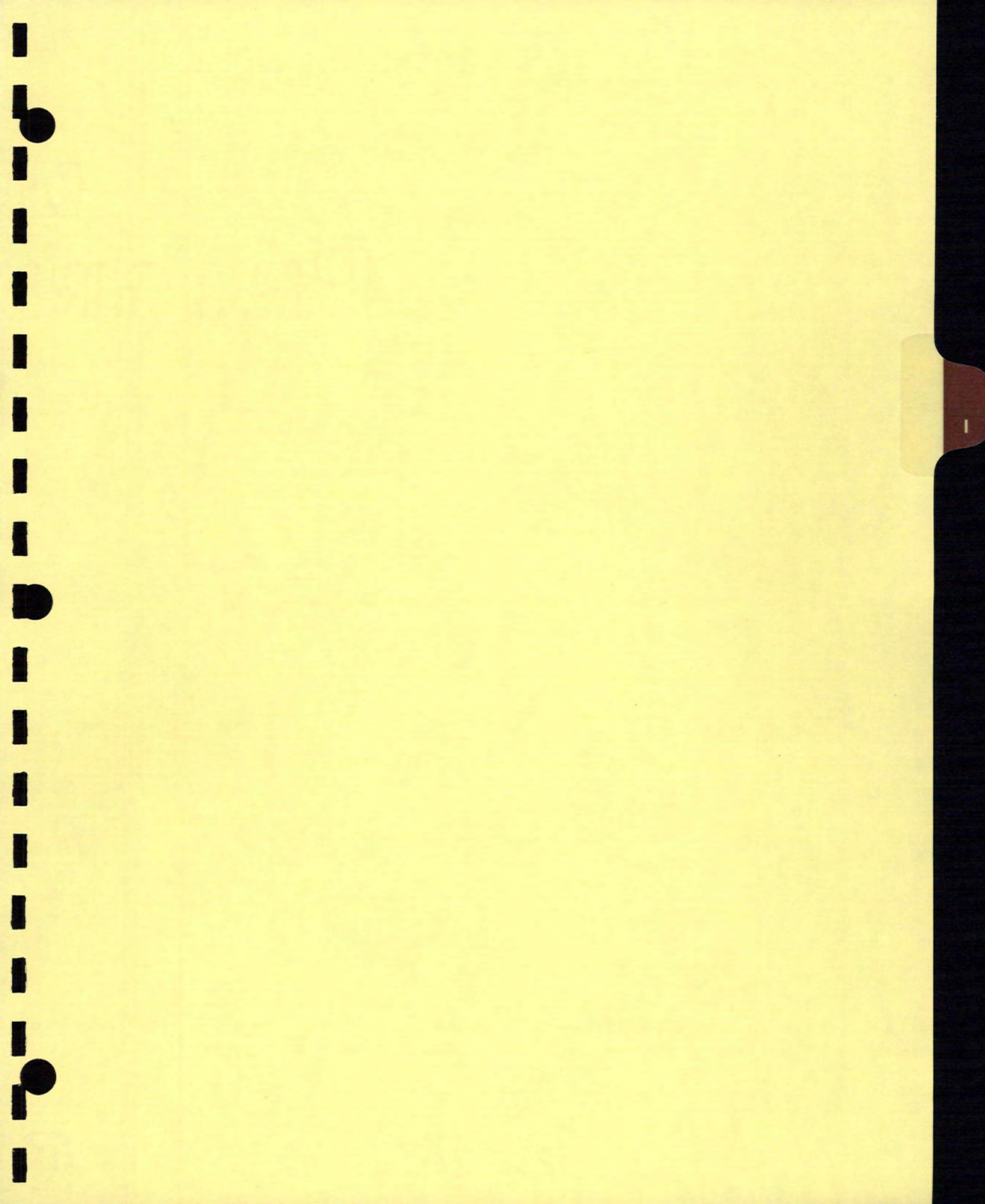
We believe this can only come about through the creation of "**partnerships for change**" and the establishment of a national agenda in which business, government and the professions are all equally committed to by the same "**vision**".



The challenge is perhaps best captured by Professor George C. Lodge in the final chapter of his book "**Perestroika for America**" where he notes that:

**"Central to this task is improved business-government relations that rest on a redefinition of the roles of each and the design of new mechanisms and procedures for bringing them together. This means change and controversy. It will take time: hopefully not too much because with time comes crisis, and crisis is expensive. It is a shame to waste it. To repeat: The overriding task of leadership in government and business is to make maximum use of minimum crisis for maximum change.**

This Report is intended to help create a framework for this change.



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