

Financial Services Flash

AIRD & BERLIS LLP
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Severance and Termination Payments Under the CCAA – Part 2

In the recent case of *Sroule et al. v. Nortel Networks Corporation et al.*, the National Automobile, Aerospace, Transportation and General Workers Union of Canada (“**CAW**”) sought an order directing certain Nortel entities (“**Nortel**”) to satisfy their obligations in respect of severance and termination payments owed to unionized and non-unionized employees.

CAW and Nortel are parties to a collective agreement which obliges Nortel to make periodic payments to unionized former employees who have retired or been terminated. Pursuant to the initial order under the *Companies’ Creditors Arrangement Act* (the “**CCAA**”) made in respect of Nortel (the “**Initial Order**”), Nortel stopped making payments to former employees as well as terminated employees for certain retirement and pension allowances as well as for statutory severance and termination payments.

On April 21, 2009, CAW and a group of former Nortel employees brought a motion for certain relief. CAW argued, pursuant to section 11.3(a) (now section 11.01) of the CCAA, that the collective agreement is a bargain between it and Nortel that ought not to be divided into separate obligations. Therefore, the compensation for services performed under it must include all of Nortel’s monetary obligations, not just those owed specifically to persons who remain actively employed. Thus, the contested periodic payments to former employees must be considered part of the compensation for services provided after January 14, 2009, and are therefore exempt from the stay order of that date by section 11.3(a) of the CCAA.

The former employees sought an order varying the Initial Order to require Nortel to pay termination pay, severance pay, vacation pay, and an amount for continuation of the Nortel benefit plans during the notice period in accordance with the *Employment Standards Act* (the “**ESA**”). The ESA sets out obligations to provide notice of termination of employment or payment in lieu of notice and severance pay. This “me too” claim was based on the position that Nortel could not contract out of their obligations under the ESA. Nortel argued that if the stay did not apply to these payments, the employees who received these payments would, in effect, be receiving a “super-priority” over other unsecured or even secured creditors.

At the Ontario Superior Court, Morawetz J. found that although the triggering of the payment obligation may have arisen after the Initial Order, it did not follow that a service had been provided after the Initial Order. Further, Morawetz J. held that section 11.3(a) contemplates some current activity by a service provider post-filing that gives rise to a payment obligation post-filing. In this case, the claims of CAW for termination and severance pay as well as the periodic payments were based on services that were provided pre-filing. The exact time of when the payment obligation crystallized was not the determining factor under section 11.3(a). Instead, the fact that the rights to payment were vested and could be enforced under earlier collective agreements indicated they were not for current services. The critical factor to apply was whether the employee performed services after the date of the Initial Order.

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The Court of Appeal upheld the decision of the lower court and dismissed the appeals. The Court held that section 11.3(a) of the CCAA should be narrowly construed so as to preclude periodic payments to former employees from the definition of “services” under this provision. The periodic payments to former employees were deferred compensation for past services rather than compensation for current services and were therefore not exempted from the stay in the Initial Order.

The Court of Appeal also considered whether the Court is entitled to extend the effect of its stay order to termination and severance payments based on the constitutional doctrine of paramountcy. The Court found that the CCAA stay provision is a clear example of a case where the intent of Parliament, to allow the Court to freeze the debt obligations owing to all creditors for past services in order to permit a company to restructure, would be frustrated if the Court’s stay order could not apply to statutory termination and severance payments owed to terminated employees in respect of past services. The Court also agreed with Nortel’s argument that if the stay did not apply to these payments, the employees who received these payments would in effect be receiving a “super-priority” over other unsecured or even secured creditors. They found that the doctrine of paramountcy applies to give the CCAA judge the authority under section 11 of the CCAA to order a stay of proceedings that has the effect of overriding section 11(5) of the ESA which requires almost immediate payment of termination and severance obligations.

Leave to appeal to the Supreme Court of Canada has since been denied.

The Financial Services Group at Aird & Berlis LLP has a great deal of experience in CCAA proceedings. For more information, please contact any member of the Financial Services Group. Details can be found on our [Financial Services, Insolvency and Restructuring web page](#), by clicking on [members](#).

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