Administrative Agreements with Receivers

This communication replaces Directive CA-91-25, reproduced as Directive 12R in the directives issued by the Office of the Superintendent in Bankruptcy, Administrative Agreements with Trustees and Receivers.

The intent of this communication is to outline the Canada Revenue Agency’s (Agency) policy for open communication and agreements between the Agency and practitioners appointed as receivers, in cases where the projected recoveries of an insolvent’s assets are insufficient to satisfy both the Crown’s priority claim(s) and the interest of a secured creditor initiating receivership action against the debtor’s assets. As the establishment of such agreements requires the use of the Crown’s funds to facilitate an insolvency process, this communication further outlines the information requirements, necessary for the Agency to complete a thorough review of each request received, prior to entering into agreements that authorize the use of Crown funds.

This policy sets out a general understanding as to when the Agency may, despite the Crown’s priority, allow the practitioner’s claim(s) to pay part of its fees and costs out of the net proceeds of realization. In cases where Crown priority is not initially identified, reasonable fees and costs relating to subsequently identified priority debt will be allowed, providing that due diligence has been exercised by the practitioner. As soon as a situation exists where a Crown priority claim has been identified, information must be provided to the Agency for pre-approval of any costs going forward. The Agency should expect to be included in any consultations between the receiver and appointing creditor, in relation to the handling of the assets, including decisions to continue operations or liquidate, which could potentially impact fees and costs being pursued with the Agency and the expected outcome.

receivership cases will normally require a customized solution and collection officers, with the assistance of their Headquarters Field Support representatives, are encouraged to work with receivers in exploring the appropriate solutions.

Further information on this subject is provided in the attached Administrative Agreements with Receivers.

Please consult your Field Support Programs Officer for any clarification you may need on this policy.

Original signed
by
D.L. Livingston (Ms.)
Director
Accounts Receivable Tax Programs
**Background**

Receiverships to which this policy applies include any proceeding started by a secured creditor either before a court or under a security agreement under which a receiver is appointed to take possession of and realize upon some or all of the assets of a debtor and distribute the proceeds to the secured creditor. In some cases, interim receivers may be appointed (through a court order) to preserve the assets of an estate or to maintain the affairs of a debtor for the benefit of some or all creditors.

Because of the Crown’s priority claim(s) against a debtor’s asset(s), secured creditors have expressed concerns about their potential financial exposure, when using the services of a receiver to enforce their security instruments against assets of a debtor. In keeping with the CRA’s policy that its priority claim attaches to the net realizable value of a debtor’s property, it is appropriate, in certain circumstances, to expand the CRA’s approach to allow reasonable fees and costs in receivership situations.

**Key Legislative Highlights**

In receivership situations, as with all other cases, the deemed trust provisions in the *Income Tax Act* include (for clarity purposes) unremitted amounts of federal and provincial tax, as well as employee contributions of Canada Pension Plan and Employment Insurance that have been deducted or withheld. However, under the *Excise Tax Act* (ETA) and the *Air Travellers Security Charge Act* (ATSCA), a deemed trust represents the amount of tax that the insolvent collected but did not send to the CRA.

Regarding Enhanced Requirements to Pay, amounts involved include the total unremitted liability of the insolvent, including federal and provincial tax deducted at source, both the employee’s and the employer’s share of CPP and EI contributions, amounts that have been collected or are collectible by the debtor (ETA/ATSCA), and any applicable penalties and interest.

**Key Focus and Issues**

In receivership situations, the focus and principles are different than in bankruptcy.

Bankruptcy involves the orderly administration of the estate to the benefit of all creditors, and fees and costs associated with the administration of an estate are derived from the realization of an insolvent’s assets. In a receivership (whether by court or private appointment), actions are taken against the secured assets of the insolvent and the responsibility for the payment of reasonable fees and costs of the receiver are borne by the party that starts the proceedings. The policy in these cases is designed to accomplish the following:
• provide a mechanism whereby fees and costs directly associated with actions taken for the CRA’s benefit are covered in receivership situations where realization results in a shortfall; and
• give the Crown a chance to maximize recovery during the receivership.

Process – General

Where an initial financial analysis shows that there will not be enough funds to pay the Crown’s priority claim and the costs of the realization of a debtor’s assets, the receiver is expected to contact the CRA at once. This contact will let the receiver outline the facts of the case, provide estimates of fees and costs anticipated with realization, and discuss the CRA’s position regarding the allowance of some or all of the costs of the realization, ahead of the payment of the Crown’s claim.

If the receiver does not contact the CRA as soon as the initial analysis confirms the need for an agreement, or if the receiver does not provide the CRA with enough supporting information, the CRA will reject a request to delay the Crown’s payment.

Due to confidentiality concerns it will be necessary for the receiver to provide the CRA with the proper authorization (Form RC59, Business Consent Form, and/or Form T1013, Third Party Authorization Form, as applicable) when making a request to the CRA to allow for a full review and response.

On receipt of a notice of a receiver’s appointment, the CRA should verify the extent of any priority claim, by completing any necessary payroll and goods and services tax/harmonized sales tax audits of a debtor’s books and records as soon as possible.

The CRA, with the help of the Department of Justice Canada as required, will determine whether an agreement should be made, consider the merits of the case, and through discussions with the practitioner, determine the appropriate terms and structure to be reached.

Unless otherwise authorized by the CRA, the proceeds of recovery of an asset should not be used to fund the recovery of more assets. For example, proceeds from the collection of accounts receivable should not be used to proceed with actions towards the recovery of other assets.
When an agreement has been reached, the receiver will have to give the CRA regular progress reports about the following:

- liquidation, realization, and disposition of the asset(s);
- anticipated fees and costs, as negotiated by the parties; and
- immediate reports of material changes or cost overruns anticipated in the realization of the assets.

Time frames will be detailed in the terms of the agreement to be sent with the CRA’s letter to the practitioner. Practitioners will not draw fees without approval from the CRA.

**Multiple Receivers**

There may be cases where multiple receivers are enforcing a security interest in relation to the various asset(s) of a client. In these instances, it will be necessary for each receiver to negotiate their respective agreements with the CRA. Where the CRA has entered into an agreement with a receiver based on the circumstances of their case, this does not imply that the terms of such an agreement will extend to agreements with other receivers.

**Other Priority Claims**

In allowing reasonable fees and costs out of the Crown’s priority claim(s), agreements for this allowance by the CRA are not binding on other creditors (including such things as construction liens claims or unpaid wage claims) holding a priority over fees and costs for the administration of the estate. To avoid potential conflicts when surplus funds are realized by a practitioner above the CRA's priority claim, the practitioner will have to negotiate with creditors holding priority over fees and costs separately. Also, the practitioner will have to make the CRA aware of this situation before approaching the organization with a request to allow reasonable fees and costs.

**Reasonable Fees and Costs**

The circumstances under which a receiver may be appointed will vary. So the allowance of reasonable fees and costs associated with the realization of assets encumbered by the Crown’s priority charges will be considered case by case.

In receivership situations, the reasonable fees and costs that may be allowed include those that are directly attributable to the realization of assets to which the Crown holds a priority claim. In particular, those expenses that relate to the receiver’s direct expense in possessing, storing, insuring, repairing, preparing for sale, and selling assets that generate deemed-trust proceeds, may be authorized.
The following are fees and costs that the CRA will not normally allow a receiver to deduct before the payment of a priority claim:
   a) basic fees and costs associated with the administration of the receivership proceedings;
   b) costs that are more than the net realizable value of the assets against which the Crown’s priority claim applies;
   c) costs of actions taken (related to the realization of asset(s)) that have resulted in direct financial benefit to other creditors;
   d) costs incurred where the CRA decided not to pursue its priority claim against the assets covered by the receivership action; and
   e) fees and costs that relate to general office expenses of the practitioner.

In rare cases, the CRA may ask the receiver for help in recovering on accounts receivables for which enhanced requirements to pay are in effect. In these situations, the CRA will cover reasonable fees and costs directly associated with recovery on the agreed-upon accounts receivables.

Where there are existing Enhanced Requirements to Pay in effect by the Agency and on issuance of any new Enhanced Requirements to Pay, where agreements with the receiver have been finalized by the Agency, a letter to third parties (see Appendix C) will be issued, outlining the action taken and directing them to forward any amounts captured to the receiver, until advised otherwise.

In certain cases, receivers can use other means to mitigate their losses, such as:
   • filing a small business loan insurance claim; or
   • third-party indemnity agreements to the receiver from the appointing secured creditor.

In cases where there is evidence of such agreements and/or claims, information regarding the circumstances and amounts recoverable from these means (if applicable) will be considered by the CRA in its decision-making process. The CRA recognizes that third-party guarantees cannot be relied upon to cover costs directly related to asset realization for the benefit of the Crown.

When priority has not been identified from the start, reasonable fees and costs relating to later-identified priority debt may be allowed, as long as due diligence has been exercised by the practitioner.

Request and Response Procedures

To allow the Agency to review and make decisions quickly in receivership situations, the specific information requirements of the practitioner, are outlined below (see letter attached at Appendix B):
   • Form RC59, Business Consent Form, and/or Form T1013, Third Party Authorization Form
• notice of appointment
• security agreement(s)
• notice of default, demand for payment, and notice of intention to enforce security
• statement of affairs
• letter of indemnity (where applicable)
• financial statements
• appraisal reports (where completed and/or available), valuation details, and type of valuation
• estimated time frame for liquidation
• summary of extraordinary items (such as conservatory measures required and time frames), where applicable

To ensure a consistent approach to handling requests for agreements between the CRA and practitioners appointed as receivers, a standardized request form (to be used by practitioners) and formal response letters (to be used by the CRA) to convey decisions and/or requests for more information, should always be used.

Formalizing this communication process will promote timeliness and completeness in review and responses to requests, and help practitioners to provide all of the necessary information.
Appendix “A” – Legislation

The Crown’s property claim(s) arises by operation of the law pursuant to the following:

<table>
<thead>
<tr>
<th>Legislative Reference</th>
<th>Trust Monies</th>
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<tbody>
<tr>
<td>Income Tax Act</td>
<td>227(4) &amp; (4.1)</td>
</tr>
<tr>
<td>Excise Tax Act</td>
<td>222(1)</td>
</tr>
<tr>
<td>Air Travellers Security Charge Act</td>
<td>15(1)</td>
</tr>
<tr>
<td>Canada Pension Plan Act</td>
<td>3(3) &amp; (4)</td>
</tr>
<tr>
<td>Employment Insurance Act</td>
<td>86(2) &amp; (2.1)</td>
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Appendix B – Request Letter for Receiverships

RE: Agreement between (representative name) and Her Majesty the Queen, in the matter of the receivership of XYZ (sometime carrying on business as XXXXX).

Please be advised that on the (date), XYZ was placed into receivership and that (representative’s name and address) has been appointed as receiver for XYZ.

Subject to verification by the Canada Revenue Agency (“Agency”), XYZ is indebted to the Agency for approximately (choose applicable liability(ies):

- (liability) of source deductions, under the account # (123456789RP).
- (liability) of Good and Services Tax/Harmonized Sales Tax (GST/HST), under the account # (123456789RT).
- (liability) of Air Traveller’s Security charge, under the account # (123456789RG).

The books and records for XYZ are located at:

(Representative’s name) has confirmed the assets over which security agreements apply and their estimated net realizable value with respect to XYZ are as follows (list all applicable assets individually):

- (Representative’s name) is seeking Agency’s consent to deduct reasonable fees and costs associated with the realization of assets, prior to the payment of amounts otherwise payable pursuant to the (1) Crown’s priority claim(s) under subsection 227(4) of the Income Tax Act, and/or (2) Crown Enhanced Requirement to Pay under subsection 224(1.2) of the Income Tax Act, subsection 317(3) of the Excise Tax Act, and/or subsection 75(3) of the Air Travellers Security Charge Act.

Based on our preliminary review, the estimated realization fees and costs, before disbursements, relating to assets to which the Agency’s priority attaches are approximately (dollar amount).

To facilitate the Agency’s review, attached please find the following information:

- Form RC59 - Business Consent Form
- Notice of Appointment
- Security Agreement(s)
- Notice of Default
- Demand for Payment
- Notice of Intention to Enforce Security
- Statement of Affairs
- Letter of indemnity (where applicable)
- Financial Statements
• Appraisal reports (where completed and/or available)
• Valuation details and type of valuation
• Estimated costs of realization per asset/category of assets (e.g. for inventory)
• Estimated timeframe for liquidation
• Summary of extraordinary items (i.e. conservatory measures required and timeframes) where applicable

Please contact our office, should you require additional information or wish to further discuss this estate.

___________________
Representative Name
Appendix “C” Enhanced Requirements to Pay

Attention:

Dear Sir:

Re:

The attached Enhanced Requirement to Pay is being issued, pursuant to subsection 224(1.2) of the Income Tax Act, to capture any funds which you have payable or may have payable to the above noted party.

The above noted party is the subject of receivership proceedings and that the authority to intercept any funds owing to this party, as provided in subsection 224(1.2) of the Income Tax Act, is not impeded by any stay of proceedings associated with those proceedings.

Further to an agreement between the Canada Revenue Agency and “insert Representative’s Name”, any amounts subject to this Enhanced Requirement to Pay are to be directed to “insert Representative’s name” until the Canada Revenue Agency provides you with other instructions.

Pursuant to subsection 224(4) of the Income Tax Act, failure to comply with the terms of this Enhanced Requirement to Pay may result in an assessment and legal action against yourself for any amount that you fail to remit to the receiver.

If you require further information with respect to this matter, please contact our office at the telephone provided in this letter.

Yours truly,