

INSOLVENCY GROUP NEWS

AN EQUIFAX COMMERCIAL INFORMATION SOLUTIONS PUBLICATION

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Insolvency News Update

Mark your Calendars for Wednesday, February 7, 2001. That is the date of the next Insolvency Group Forum in Toronto. Our featured speaker will be David Stewart, the Associate Superintendent of Bankruptcy. Mr. Stewart is a dynamic speaker and is recognized as a leading authority on insolvency matters. Most important, however, he is a key participant in the revision process for the Bankruptcy and Insolvency Act in 2002.

We are anticipating a full day of value-packed information sessions. From informative presentations and member-only discussions to a question and answer period with the Superintendent of Bankruptcy, you will be glad you attended. And remember, all of this, plus a delicious lunch, are included in your annual fee as members of the Equifax Insolvency Group.

The purpose of the group is to give direction to and support the lobbying efforts required to make changes to the BIA. If you are not a member, we invite you to join. You will receive newsletters and other printed materials as well as information to attend special meetings.

To join, simply fill out the attached application form and return it to Bob Rose by facsimile at (416) 227-5394 or email: bob.rose@equifax.com. ♦

The Right to Restructure

*Melvin C. Zwaig, President and CEO, and
Michelle Pickett, Consultant Zwaig Consulting Inc., Toronto*

What are the criteria for determining if a company should be allowed court protection to restructure? Who should decide if a company should be allowed to restructure?

Clearly, these are critical issues, particularly given the number of companies that seek court protection from their creditors for a second and even a third time – including such high-profile examples as Eaton's and Agnew Shoes, as discussed below.

We may well ask: Is the present system working? From our perspective, the answer is No. We propose that, to strengthen the system, a strategic analysis should be an essential requirement for any business in seeking court protection.

The Current System

We currently rely on our judicial system, specifically commercial court judges, to decide which companies are worthy of court protection from their creditors while they restructure their operations. The Court basis its decision on an analysis prepared by the company and its legal team, focusing on the financial

plight of the debtor as well as the social and economic impact of job losses if the company is liquidated. The underlying premise is that, if a company can find financial relief from its creditors, then it can be successfully restructured.

However, what about the company that is facing a financial crisis because of operational or business issues? Can this company be successfully restructured by granting it temporary asylum from paying its creditors?

The streamlined process outlined above is far too limited in this instance. It ignores many factors that should be considered in determining whether a company can be successfully restructured. This includes the future potential of a business, which should be the primary consideration of any decision to restructure. This potential can be assessed via a strategic analysis of the business, which would include not only an examination of the business itself, but the industry in which it operates and the economy.

Industry Analysis

An analysis of the debtor's industry would entail a review of such factors as competition, cost structure, product life

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**Reserve your seat now
Insolvency Group Meeting
with David Stewart
February 7, 2001 – The Old Mill, Toronto
See Page 4 for details**

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cycle, supplier and buyer power, supply and demand. It would also include any external factors affecting the industry, such as the economy, consumer trends and fads, technological changes and any political and governmental policies, such as free trade.

Business Analysis

An analysis of the business would focus on supply and demand for the company's products and the company's position in the industry, including its market share, cost structure, marketing, marketing prowess and management strength or weaknesses.

Economic Analysis

The economic analysis is related to the industry analysis: the health of the economy has a direct impact on the strength and attractiveness of the industry, acting as a bellwether of its future potential. An economic analysis would consider many different factors, including GDP growth, consumer spending, consumer confidence, business investment, retail sales, unemployment rate and inflation.

To consider the impact and value of a strategic analysis, one need only be reminded of the following cases.

Horse and Buggy

Would it have made sense to restructure a horse-and-buggy dealer following the invention of the automobile? While hindsight is 20/20, an in-depth analysis of this business would have revealed that its days were numbered. The industry was changing and, as consumers sought the faster, smoother ride of an automobile and demand waned for the horse and buggy, the company would continue to lose market share.

The T. Eaton Company

A strategic analysis of the retail industry and Eaton's position in it would have indicated that the company's weak market and financial positions left it in a precarious spot from which to compete.

The T. Eaton Company suffered from many years of store neglect and bad management. As a result, it lost considerable market share to The Bay, Zellers, Sears and Wal-Mart. At the time of its initial filing for court protection under the Companies Creditors Arrangement Act (CCAA) in February 1997, it reported losses of \$170.1 million for the fiscal year ended January 25, 1997. At this juncture, at least one-third of its stores were unprofitable, and all stores required extensive upgrade renovations to make them customer friendly.

In its initial restructuring under CCAA, Eaton's honoured its obligations, and all creditors were repaid in full. This occurred despite incurring extensive professional fees. Obviously there was significant value remaining in the organization.

Creditors did not fare well under the second restructuring, realizing only 50.3% of the value of their unsecured debt due from Eaton's. Despite raising \$175MM in equity from the public market, the new management of Eaton's could not return the company to profitability. The magnitude of neglect at the store level and management level could not be corrected in the time period allowed. Eaton's faced an uphill battle trying to regain lost market share in a short time period.

Agnew Shoes

Again, while hindsight is 20/20, a strategic analysis of Agnew would have revealed that it had a weak position in the market and that it was being squeezed out by low-cost and low-price competitors such as Wal-Mart and Payless Shoes. Furthermore, Agnew was under-capitalized, which left it in a precarious position in the event of a hiccup in sales or margins.

Agnew Shoes is presently engaged in its third court restructuring. In both of the prior restructurings, the unsecured creditors incurred large losses. Was it a good decision to grant Agnew court protection from its creditors a second or

third time, when all of its competitors in the middle market had exited the business?

Who is Responsible?

Having determined that a strategic analysis is necessary in any court decision to grant a company protection from its creditors, who then is responsible for performing the analysis? Is the court responsible, or is the company responsible?

It may be argued that preparing such an analysis is not the responsibility of the court, notwithstanding that it would be a useful tool in decision making. What about the debtor? Should the debtor be responsible for preparing such an analysis? Certainly it would be a useful exercise, one that might well assist management in determining if and how it can restructure the business.

Benefits of a Strategic Analysis

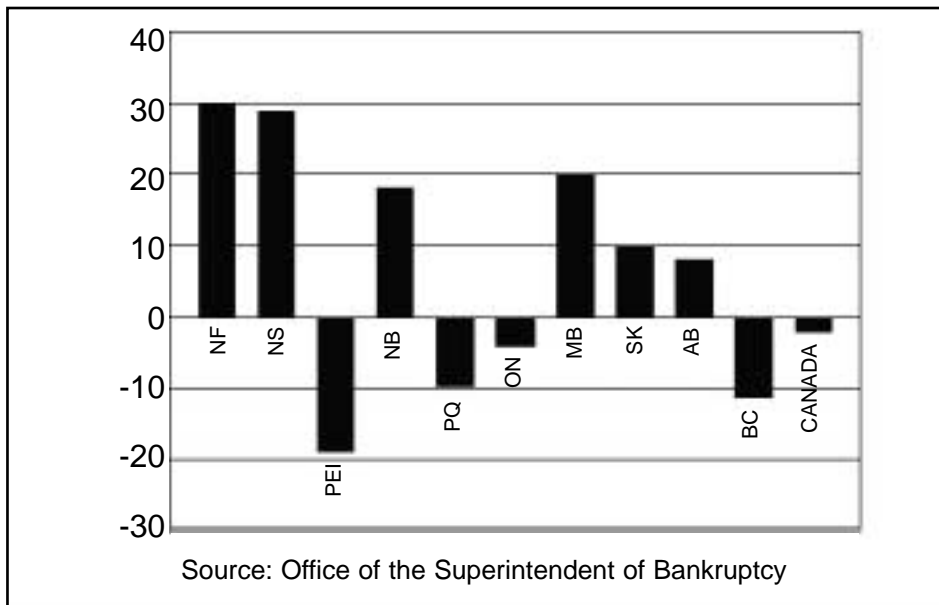
We propose that a strategic analysis of a business be a required component of any application to the court for protection from a debtor's creditors. The benefits of such an analysis would have a three-fold impact:

- It would enable the court to make a more informed decision on which companies are worthy of court protection while they attempt to restructure their operations
- Debtors would be forced to conduct an in-depth analysis of their businesses, which should prove quite useful in their restructuring plan; and
- Creditors would have better information with which to decide if they want to support or extend debt to the debtor in the future.

Editor's note: Melvin C. Zwaig is the founding member of Zwaig Consulting Inc., a Toronto financial management consulting firm that specializes in turnarounds and statutory insolvency services.

Bankruptcy Statistics

Percent Change January-June 1999 – January-June 2000



From the East coast to the West the Bankruptcy numbers bear out an interesting landscape. Although the overall number of business bankruptcies in Canada decreased by about 2.4% over this period, the distribution was not equal. There was a 2.6% increase in the west coast and an 18.1% surge in the Maritimes. The Canadian average was brought in line by an overall decrease of 7.3% in Ontario and Quebec.

Where will your next Bankruptcy appear? Dealing with a bankrupt

customer seems to be an inevitable part of doing business. As credit professionals we must not only be adept at facing these situations, we must also look for ways to improve our recoveries in general. Positive change to existing legislation is the only long-term remedy to ensure our success. Our Insolvency Group is a unique vehicle to bring the interests of unsecured creditors to the attention of those who make change happen. Get involved, be a part of the process for Change. Spread the word. ♦

Your Thoughts Matter...

If the saga of the US presidential election hasn't made you stop and think about the power of a single vote...

Whether you choose to speak up at a meeting or voice your opinion over the telephone, we want to hear from you. And if you prefer to put pen to paper, great. We would be glad to include your submission in our next newsletter.

The Insolvency Group wants to make things happen. Direct your comments to Bob Rose at 416 227 5322 or email me at bob.rose@equifax.com. ♦

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In the next issue...

- A review of the Credit Institute of Canada's "The Bankruptcy and Insolvency Act of Canada – A Creditor's Perspective" which has been recently endorsed by the Superintendent's office.
- "The Right to Restructure" – a follow-up story from Mel Zwaig.
- The full agenda of the February 7, 2001, meeting with the Associate Superintendent of Bankruptcy.

... available January 2001

WE ENCOURAGE YOU TO MAKE COPIES OF THIS NEWSLETTER.
SHARE IT WITH ANYONE INTERESTED IN SEEING
CHANGES MADE TO THE BIA

A Meeting with the Superintendent of Bankruptcy Reservation Form

Wednesday, February 7, 2001 – 9:30 a.m. to 3:30 p.m.

The Old Mill
Toronto, Ontario

Please complete the following and fax it to 416 227 5394

Insolvency Group Members – Free Non-Insolvency Group Members – \$150
Refreshments and lunch are included

- Please contact us; we are interested in finding out more about this group.
 I am a member of the Insolvency Group and will be attending.
 I am not a member of the Insolvency Group but will be attending.

Please charge my Equifax Account Number _____

Name _____ Title _____

Company _____

Address _____

Telephone _____ Fax _____

Email _____

Signature _____

The Insolvency Group Needs You

The Insolvency Group's purpose is to make positive changes to existing insolvency legislation. To effectively lobby the Superintendent of Bankruptcy, we need broad industry representation and a strong voice to put forward recommendations. If you support our initiative, then please join the Insolvency Group now – Annual fee of \$400.

**Come out on February 7 – and if you decide to join then,
we'll apply your entire meeting fee to your Insolvency Group membership of \$400.**

INSOLVENCY GROUP NEWS

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