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Bankrupt firms tapped federal wage subsidy despite long odds of survival

TOM CARDOSO AND PATRICK BRETHOUR

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The federal wage subsidy program, aimed at preserving jobs during the pandemic, was designed so broadly that bankrupt businesses in the process of winding up their operations were able to access it, a Globe and Mail analysis has found.

Dozens of companies that filed for bankruptcy before the pandemic – and dozens more afterward – received the Canada Emergency Wage Subsidy (CEWS). But bankrupt companies, which by definition are in the process of closing their business, were already planning on laying off all their workers, meaning their CEWS-subsidized jobs were likely unsalvageable in the first place.

By cross-referencing the CEWS registry and data from the Office of the Superintendent of Bankruptcy, The Globe identified 32 companies with liabilities totalling $11.3-million that filed for bankruptcy between January, 2019 and March 11, 2020. That was the day the World Health Organization declared a global pandemic. Another 130 companies – with liabilities totalling $332.5-million, and that filed for bankruptcy some time between March 12 and the end of 2020 – also received CEWS.

Troubling questions about Ottawa’s pandemic wage subsidy program, CEWS

During bankruptcy, a business – often administered by an appointed third-party such as an accounting firm – sums up its assets and pays out as many creditors as it can before shutting down, a process known as “liquidation.”

The Globe’s findings raise questions about the design and broad eligibility requirements for CEWS, which the government estimates will cost $110.6-billion by the time it ends this fall. Despite the program being promoted as a way to save jobs, most positions at bankrupt companies were doomed from the start, and federal funds may well have ended up with those companies’ creditors.

“If the purported goal of CEWS is to save jobs and you’re liquidating anyway, no jobs are being saved,” said Joel Blit, an economics professor at the University of Waterloo who studies innovation.

CEWS payments are reimbursements for payroll expenses already incurred, and the intent of the program is to allow struggling companies to continue to pay wages. However, Prof. Blit said that bankrupt companies could instead earmark their payments to paying off creditors. “It’s a direct transfer from the government – from taxpayers – to the people holding the debt for these companies.”

The analysis points to a lack of targeting, he said, with the CEWS program ultimately subsidizing companies whose troubles had little to do with the pandemic.

The list of bankrupt companies includes sporting-goods stores, food-service establishments and construction companies – mostly small, local businesses that went belly-up in the months before the pandemic.

Last week, a Globe investigation identified hundreds of publicly traded companies that, combined, received at least $3.6-billion in CEWS payments. Many of those companies actually saw increased revenues during the pandemic.

The tally of bankrupt businesses receiving CEWS does not encompass those in other states of insolvency. Regional airline Air Georgian Ltd., for instance, began as a restructuring before moving into bankruptcy. And Bondfield Construction Co. Ltd., a major Ontario-based construction company, has accessed the CEWS program while under a years-long restructuring process.

It isn’t possible to know how much each bankrupt company collected since the government does not publish individual CEWS receipt data. Given that Ottawa has published only the names of companies that took CEWS, the analysis relied on company names to identify subsidy recipients, which could lead to incorrect matches. To account for this, the list was manually examined. Businesses with common names, such as popular franchised eateries or pharmacies that share a brand name, were removed.

Prof. Blit, the University of Waterloo economics professor, argues that economic downturns figuratively set the business landscape ablaze and kill off the less successful companies, allowing new ones to grow in their place. The CEWS program interrupted that process, Prof. Blit said. According to the Bank of Canada, insolvency filings in 2020 declined by nearly 25 per cent compared with 2019.

“I’m not saying there shouldn’t have been any support,” Prof. Blit continued, “but the question is, was it too generous? Did we work so hard at maintaining the status quo that we didn’t allow this churn in our economy that is healthy?”

Before the pandemic, small airline Air Georgian had already taken a blow to its business. For years, it had subcontracted for Air Canada, logging short-haul domestic and Canada-U.S. flights. But in 2019, Air Canada told the company it was ending the contract, and with it Air Georgian’s main source of revenue. By November, 2019, nearly all its pilots and flight attendants had been laid off.

After spending much of 2019 and early 2020 looking for a buyer, Air Georgian began insolvency proceedings; in a February filing, accounting firm KPMG listed $44.7-million in claims from creditors. But on March 9, 2020 – two days before COVID-19 was declared a pandemic – Air Georgian finally found a buyer. Two months later, the business was sold.

In any other year, this would have been just another bankruptcy. But Air Georgian – an airline with virtually no pilots or flight attendants, and that was effectively bankrupt by early March – accessed CEWS, according to the government's registry of recipients.

Despite its insolvent status, there is no evidence that Air Georgian was ineligible for the federal program or otherwise did anything untoward. In fact, a KPMG trustee specifically mentioned CEWS in an April report, saying Air Georgian was "hopeful" that it would qualify for the program.

The trustee added that if the company received CEWS, it might increase its cash receipts – money that could be used to pay off creditors. (Air Georgian's trustee did not respond to The Globe's requests for comment, nor did the business's new owner, Pivot Airlines.)

Daniel Weisz, a partner and senior vice-president with the restructuring and recovery practice of accounting firm RSM Canada, said it would be unusual for a company in restructuring to turn down an opportunity to access a source of cash.

However, there could be issues if a company with a pending CEWS application went bankrupt. If a trustee received such a payment, it would be prudent to contact the government, Mr. Weisz said, since it is possible that Ottawa could demand repayment, even without a specific prohibition in the legislation governing the CEWS program.

"That's not set out anywhere in there, but I think we both know that the government could use whatever bit of money it could get," he said. "And it hasn't been exactly diligent in determining where the money has been going."

David Ullmann, a partner at law firm Blaney McMurtry LLP and expert on insolvencies, said he and his colleagues wondered early on if insolvent companies might be eligible for CEWS. "When we looked at it, we didn't find anything in the program that prohibited a company that was insolvent from filing," he said.

"If the program cast a wider net than maybe the government wished it did," Mr. Ullmann said, "that's not the fault of the people who then use the program, in my view."

In an e-mailed statement, Katherine Cuplinskas, a spokesperson for Finance Minister Chrystia Freeland, did not directly answer questions about whether companies already undergoing bankruptcy proceedings were or should be eligible for the program.

Bondfield Construction, another company in insolvency proceedings, has also received CEWS, according to the federal government's registry, as did 352021 Ontario Ltd., a

Bondfield-related company. The construction company has been embroiled in a restructuring since 2019.

Alan Merskey, a lawyer with Norton Rose Fulbright Canada LLP, which is representing the court-appointed monitor for Bondfield, confirmed that the company received CEWS for its construction and administrative staff. While under restructuring, Bondfield has continued to operate as a general contractor on a number of projects.

For Michael Smart, an economics professor at the University of Toronto who has examined CEWS, the fact that bankrupt companies have claimed the subsidy raises several questions. The first, he said, is whether they are truly eligible, or if there's an issue at the Canada Revenue Agency in determining their eligibility. Second is whether this is a good use of government funds in the first place.

"If the firm is no longer operating, then there is no sense in which CEWS could be saving jobs," Prof. Smart said. "So the existence of these cases tells me there's a problem with program eligibility and program design."

https://www.theglobeandmail.com/business/article-bankrupt-firms-tapped-federal-wage-subsidy-despite-long-odds-of/