

Pension Planning

September 2005

Managing Your Group RRSP

No longer a turnkey matter

Your business is firmly established, and you are in it for the long term so you want to establish a Group RRSP for your employees to reward their loyalty and to help them with their financial planning. You have obtained quotations from several insurance companies and investment dealers, and interviewed two or three and selected insurance companies as your provider. You have decided on the level of matching employer contributions on the basis of what is normal for companies of your size. You have provided a large number of investment options for members to choose. You set up an introductory meeting between the RRSP provider and your employees during business hours to explain the Plan. Your payroll programme is set up to make the deductions for any employee who joins.

You have done your best for your employees. There is nothing more to do. Right?

Not quite. There are new guidelines issued by the Joint Forum of Financial Market Regulators which will come into effect at the end of 2005. Those guidelines will apply to capital accumulation plans (CAP) such as Group RRSPs as well as to registered defined contribution pension plans.

The CAP Guidelines create a standard of good practice that you will want to be sure you have adhered to for your own protection.

Remember, it is not when things go right that you are exposed to lawsuits from employees and former employees. It is when are dealing with a terminated employee who feels aggrieved, or when the stock market has taken a downturn and employee's expectations (reasonable or not) have for some reason not been met.

What can you do to insure that your Group RRSP is properly managed?

Priscilla Healy, a leading Canadian pension lawyer with special expertise with the CAP Guidelines, has recently joined Palletts. She has been personally involved in the development of the CAP Guidelines through industry committees. Given the new CAP Guidelines, we recommend that you spend some time reviewing your Group RRSP with Priscilla, and with your service provider.

You have provided a valuable service to your employees. We can get you to be comfortable that you have maximized the benefit to them and minimized the risk to your company.

Questions to ask about your Group RRSP

- **Have I selected investment choice options which are appropriate for my mix of employees?**
- **Have I adequately communicated the default option to my employees?**
- **Are the illustrations as to investment returns realistic?**
- **How clearly will my employees understand their risks and responsibilities?**
- **Do my employees understand the fees and expenses they are paying?**
- **Should I be offering financial planning to my employees?**
- **How closely do I need to monitor my service provider?**

An expanded list of issues to consider can be sent to you before your meeting with Priscilla Healy.

Ontario's Pension Benefit Guarantee Fund (PBGF)

It has been in the news during the Stelco insolvency and if your business has a registered Ontario pension plan you are paying for it every year. What does it do?

The PBGF is a fund made up of annual dues (which are called assessments) from all employers with defined benefit plans that have members working in Ontario. The assessments are payable even if the plan is legally registered outside Ontario.

How much are the annual assessments?

Normally the assessment is \$1.00 per member, including deferred vested members and retirees. That assessment can increase if the plan is not fully funded.

Can PBGF assessments be paid from the pension plan?

PBGF assessments can only be paid from the plan if the plan is fully funded.

What does the PBGF do?

When a defined benefit pension plan is wound up with an insolvent employer who cannot fully fund the pension plan, the PBGF will pay a portion of the pension deficit.

How much does the PBGF pay to a plan member?

Only the first \$1,000 of pension income per month is fully protected. Take the example of a monthly pension of \$2,000, and a plan that is 80% funded. Without the PBGF the member would receive only 80% of \$2,000, or \$1,600 per month from the plan. But the PBGF will top up the first \$1,000. On the first \$1,000 of pension payments, the member would receive \$800 from the plan, and \$200 from the PBGF. The member then would still receive \$1,600 per month from the plan, but would also receive \$200 from the PBGF, for a total of \$1,800 per month.

Can employees who are not employed in Ontario claim against the PBGF?

No. Only members employed in Ontario. This includes members who retired or became deferred vested members when they were employed in Ontario, even if they have since moved out of Ontario.

Recent Cases

Trust Protection in Bankruptcy

In GMAC Commercial Credit Corp. - Canada v. TCT Logistics Inc., the anxiety over the status of trust protection in bankruptcy has been put to rest by the Ontario Court of Appeal.

The Ontario Court of Appeal recently reversed, in part, a controversial lower court decision involving deemed trusts in bankruptcy. "Deemed trusts" are a statutory device imposed by legislation to ensure that companies do not avoid revenue and societal obligations, such as amounts that companies are required to deduct for registered pension plans. Deemed trusts try to avoid the requirement under general trust law that the property must be identifiable as being held in trust, and not mixed with other property. The problem with deemed trusts is that they are not recognized in bankruptcy unless they meet all requirements under standard trust law.

TCT Logistics Inc. ("TCT Logistics") operated in the truck transportation sector as a load broker (the intermediary between the carrier and those shipping product). Ontario regulations require that a load broker hold in trust money it receives from its customers that relate to fees of the carrier that actually hauled the load. When TCT Logistics went bankrupt, unpaid carriers tried to get their fees by arguing they were trust funds not affected by the bankruptcy. TCT Logistics did not maintain a separate trust account, but a lower court found that the deemed trust still had priority over the secured creditor of TCT Logistics and survived bankruptcy anyway. This excited much comment from insolvency lawyers and much excitement from those acting for "wronged" trust beneficiaries.

That excitement has largely been put to rest by the Ontario Court of Appeal, which held that the deemed trust imposed on load brokers did not survive bankruptcy, unless such trust would otherwise satisfy standard trust law principles.

We therefore strongly advise that any pension contributions, vacation pay or other employee amounts which legislation treats as trust funds should either be paid over or at least held in a separate trust account. Now that such deemed trusts are nullified, the unpaid liability could well fall back on company directors or officers.

Now, the really interesting questions

Is there enough money in the PBGF to cover the known insolvencies?

No. According to the audited financial statements of the PBGF, the PBGF had a significant deficit as of March 31, 2004. It has borrowed \$330 million from the Government of Ontario to pay for Algoma Steel and other claims against the PBGF.

How can the PBGF owe the Ontario government anything?

If there is not enough money in the PBGF to pay the benefits, the Government of Ontario may, but is not required to, lend sufficient monies to the PBGF to pay the benefits.

Is there an equivalent to the PBGF in any other Canadian jurisdiction?

The U.S. has the Pension Benefits Guarantee Corporation, but there is no equivalent to the PBGF elsewhere in Canada. There is however, discussion as to possible insurance scheme in the federal jurisdiction. We can expect significant comment from all stakeholders if such a scheme were to be seriously proposed. It is a difficult balance for any government to weigh the protection of pension plan members against the resulting burden on either “good” employers or taxpayers generally.

What is the future of the Pension Benefits Guarantee Fund?

Whenever there is a looming insolvency of a large pension plan, such as Stelco, the Government is under pressure to increase the PBGF coverage. But the PBGF has very often proved insufficient to meet its obligations.

The Government is obviously not anxious to increase PBGF premiums which will have to be paid by reluctant employers. But employers who are not insolvent would have to bear the costs of insolvent employers. Successful employers are not at all anxious to pay for failing employers, especially if they are competitors.

The alternative however is to back the PBGF with taxpayer money. But is it fair to ask a taxpayer who has no pension plan to top up the pension plan of someone else?

Pension Deduction Trusts Which Can Still Survive a Bankruptcy

*What if the standard trust principles are met? The Ontario Superior Court recently held in *Re Graphicshoppe Ltd.* that calculable pension contributions deducted from the payroll of the employees of a bankrupt company, but not remitted, could still be trust funds under ordinary trust law principles.*

Graphicshoppe Ltd. had established a defined contribution pension plan for its employees, funded by payroll deductions of 4% and employer contributions of 1%. The company was required to remit the contributions to the pension plan within 30 days after the end of the month for which contributions were payable.

Unfortunately, the company went bankrupt having deducted \$92,889.45 from the employees’ remuneration for their pension contribution, without remitting them to the pension plan. On the date of bankruptcy, the company account had a balance of \$145,667.51, but none of that was the employees’ pension contribution – it had previously been spent on company operations.

The employees argued that their pension contributions were impressed with a common law trust (not a deemed trust) and therefore were excluded from the bankruptcy. The trustee in bankruptcy argued that any trust the employees had was destroyed, because the money belonging to the employees had been spent by the company in its dying days.

The Bankruptcy Registrar held that the money was still identifiable.

On appeal, the Court accepted this but stated that the real issue was to whether the employees had any claim to the money which remained in the bank account. It decided to allocate the loss on a basis “more just, convenient and equitable in the circumstances”. The employees were wronged trust beneficiaries who should not be prejudiced by the employer’s failure to segregate their pension funds. It did not matter that the funds in the account came in from elsewhere after the trust money had all been spent.

The decision is under further appeal to the Ontario Court of Appeal.

Contact Members of the Pension Group at Pallett Valo LLP

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Priscilla Healy heads up the firm's Pension Law Group.

Priscilla practices in the area of pensions and retirement law, as well as group benefits, by themselves and ancillary to the firm's insolvency and corporate restructuring practice. Retirement arrangements for employees that include registered and supplementary pension plans and Group RRSP's, are highly regulated under provincial pension legislation as well as the Income Tax Act.

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John practices in the area of insolvency, commercial reorganization and secured financing transactions.

John has also developed specialized expertise regarding the pension and benefit plans of enterprises undergoing financial restructuring.

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Michael works closely with John Varley and other members of the firm's Insolvency and Corporate Restructuring Group and the Pension Group, to assist clients with a wide variety of matters, including the employment, benefits and pension law issues which arise on corporate liquidations or restructurings.

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Kit is a registered Trust and Estate Practitioner. She has done extensive estate planning work for both advisors and their clients while at a major Canadian trust company and two world-class life insurance companies.

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Andy practices exclusively in the area of management-side Labour and Employment Law. He assists corporate clients with a wide range of legal issues, including Employment Standards Act issues, employment and consulting contracts, workplace privacy issues, collective agreement interpretation, workplace safety and insurance issues, occupational health and safety and wrongful dismissal litigation.

The members of the Pension Group work closely with the Insolvency and Corporate Restructuring Group with respect to the restructuring of pensions and other retirement or savings arrangements.

Pallett Valo, LLP is a full service law firm with the talent, expertise, business sense and resources to handle sophisticated commercial transactions and complex litigation. We also have well established alliances with other professional services firms in order to better support our clients' business growth and personal success. Our areas of expertise include:

- Commercial Litigation
- Commercial Real Estate
- Construction
- Corporate
- Insolvency and Corporate Restructuring
- Labour and Employment
- Mergers and Acquisitions
- Pensions
- Wills, Estates and Trusts

This article provides information of a general nature only and should not be relied upon as professional advice in any particular context. For more information about pensions, contact a member of our **Pension Group** at **905-273-3300**.

If you would like additional copies of the newsletter, or know of anyone who would be interested in joining our mailing list, please contact **Jenny Chiu** at **jchiu@pallettvalo.com**.