

## Pension Update

April 2007

### Pension Plan Governance: Time for Spring Cleaning?

Up until recently, your defined benefit pension plan seems to have operated smoothly enough. You have not been affected by low interest rates of the past few years, or you have swallowed hard and dealt with the funding problems caused by them. But you have noticed signs of unease.

#### Signs and Portents

With the aging of our workforce and greater awareness of pension matters, many pension plan members are taking an active interest in the plan, by asking for a role in the governance of the plan, or pressing for a money purchase arrangement. Members may even be complaining about their contributions to the plan (and the company's contributions).

Perhaps members of your Board or your Board's Pension Committee are asking questions. They are concerned about insurance and personal liability indemnities. They could be worried about the investment of the pension fund in derivative instruments that they do not understand.

Or the regulators are taking an interest in your plan. You have received a letter from the Financial Services Commission implying your investment policy may not be appropriate, given the plan's solvency deficit; or they are urging you to address the surplus issues arising from a partial wind up that occurred years ago.

When nudged by the restiveness of the members, the board, or the regulators, it occurs to you that you don't have a written contract with your actuary or your investment manager. You are operating under a trust agreement that no one has looked at for years. Or maybe there's a draft around but it has never been signed. Come to think of it, the staff member who always understood how the plan is administered is now retired. And you've never had legal counsel or your actuary carry out a governance review.

Other matters that may be calling out for a tidy up:

- Your Statement of Investment Policies and Goals has not been updated for years;
- A past amendment to the Plan has never been finalized and filed;
- You're not sure if your pension records are backed up (or if the back-ups are kept somewhere off-site);
- Your pension records are kept in an unlocked filing cabinet near the water cooler;
- You could not find any record for an individual who

terminated employment 20 years ago and claims to have a deferred pension;

- Your new actuary has been complaining about poor data;
- You've read there may be some problem with paying expenses from the Plan (which you have been doing for years).

#### Who Will Ever Know?

If all this sounds unduly picky or even alarmist, it's not. These issues can and do come up. They tend to rear up and bite when there is a sale of a business and you have been asked for a certificate of compliance. But there are other situations where questions will be asked. For example, expect to explain your governance procedures if you propose a plan merger to which plan members object to the point of complaining to FSCO and retaining counsel.

Other situations where you can expect questions include a wind up or partial wind up and a surplus withdrawal, where counsel for the members goes looking for all the skeletons in your closet. And you will certainly be defending the governance of your plan if the solvency of your Plan goes south and first FSCO and then the members start looking around for someone to blame – and to sue. Watch out if there is an allegation of (or there has in fact been) imprudent or inappropriate or non-arm's length investments using pension funds, or for whatever reason the Plan member or beneficiaries retain legal counsel to advise about claims under the Plan.

#### Personal Liability – the Spur to Good Governance

The question of personal liability of directors and officers tends to arise particularly in insolvency situations where the members and regulators are looking around for someone to blame. Remember, directors and officers can always be prosecuted or sued for a breach of the standard of care in Sections 22(1) and (2) of the *Pension Benefits Act (Ontario)*, which can apply to senior staff as agents of the plan administrator as well as to the plan administrator (usually the company) itself. By the time there is insolvency, it is too late to remedy past omissions.

## Current Issues in Plan Governance

Current issues in plan governance include the payment of expenses from the pension fund. The Ontario courts have recently held that the payment of expenses from the Plan could be in breach of the pension trust, depending on the language in the historic Plan and trust documents. Plan administrators also have to be aware of privacy issues with the new Protection of Privacy legislation, and should have a policy for record retention. Pension plans are forever, or so it seems when it comes to record retention. And there are the larger issues requiring legal review, including whether the plan permits contribution holidays, or whether your plan can be merged with another.

## CAPSA Governance Guidelines

Governance Guidelines have been issued by the Canadian Association of Pension Supervisory Authorities (“CAPSA”). Such Guidelines are imperfect. A pension plan could be governed well and run well in practice and still be in breach of the Guidelines. But it is best to protect yourself against allegations of breach of duty by either ensuring compliance, or being in a position to explain to a regulator or the court why

the Governance of your plan departs from the Guidelines but still works well. Consider taking the useful self-assessment questionnaire in the Guidelines which can reveal gaps in knowledge or procedures.

## Good for You and Your Plan

Even without external pressure, there are good reasons for considering governance issues in the normal course of business. Good plan governance saves money through improved administration of the plan and the fund; the risk of mismatching of investments and Plan liabilities is reduced; the personal liability of the directors, officers and staff are minimized; and you save embarrassment with the members or regulators. Where there is good communication plan members appreciate better what is a very valuable employment benefit.

If several of the warning signs or concerns raised in this article are present, we suggest you consult specialist pension legal counsel to help remedy your particular problem(s), and set up systems and procedures to avoid recurrences. This is prudent pension plan administration, and you, the directors and officers of your company, the senior staff and the Board will sleep better at night.

## Pallett Valo LLP Pension Law Group

The Pallett Valo Pension Group has the senior counsel experience and capability to deal with all aspects of the establishment, operation and dissolution of pension plans. These can include plan mergers, asset transfers, surplus management and withdrawal, partial wind-up issues, as well as employer-sponsored retirement or savings arrangements (savings plans, Group RRSPs, defined contribution plans, defined benefit plans and executive supplementary arrangements). Recent regulatory guidelines governing capital accumulation plans have added a layer of complexity to these arrangements. We also advise and help develop compliance and good governance procedures in accordance with best practices to minimize liability of employers, administrators and custodians.

The members of the Pension Group work closely with the Pallett Valo Insolvency and Corporate Restructuring Group for the restructuring of pensions and other retirement or savings arrangements, and with respect to employee medical and insurance benefits.

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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 bulletin, or know of anyone who would be interested in joining our mailing list, please contact **Jenny Chiu** at **jchiu@pallettvalo.com**.