TORYS

Troubled Plans and Troubled Plan Sponsors

Legal, Actuarial and Regulatory Approaches

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“Talking about pensions may seem deadly boring but it will likely emerge as a much bigger issue in the years to come. . . . Pensions will be the biggest social issue that we’re going to be debating in our society over the next 10 years.”

Toronto Star, May 13, 2011

AGENDA

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- Introduction and definitions
- Statutory landscape
- Contributions during employer financial hardship
- Key cases
- Recent insolvency proceedings

Definitions

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- Solvency Valuations: describe plan assets + liabilities as if plan terminated/wound-up on valuation date
- Going Concern Valuations: describe plan assets + liabilities on assumption plan will continue indefinitely
- Normal Cost: current service cost of funding pension benefits in particular year
- Special Payment: contribution required to liquidate any going-concern unfunded liability/solvency deficiency

Definitions

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- *Companies' Creditors Arrangement Act* ("CCAA"): federal restructuring legislation, generally used to obtain creditor protection while restructuring a business
  - temporary protective measure
  - employer usually continues to operate
- *Bankruptcy and Insolvency Act* ("BIA"): federal bankruptcy legislation, generally used to make proposals to creditors, file for bankruptcy or appoint a receiver
  - if proposal to creditors fails, company is deemed bankrupt

Introduction

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- Registered pension plan **must be "pre-funded"**, cannot be pay-as-you-go arrangement
  - Funding
    - Central to regulatory scheme established by Ontario Pension Benefits Act ("PBA")
    - **Enhances security** of pension benefits for members
- Statutory solvency requirements: apply mostly to defined benefit ("DB") plans outside of Quebec
  - DB plan funding - uses actuarial costs methods/assumptions to create **current service cost**
  - Defined contribution ("DC") plans - fully funded once employer's normal contributions remitted

Statutory Landscape – Plan Contributions

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- Ontario PBA: strict rules for remittance of employer contributions
  - **Funding** – employer must fund pension benefits as prescribed by regulations
  - **Timing** – employer “normal cost” contributions remitted **within 30 days** of end of month contributions deducted
  - **Interest** – employer’s contributions accrue interest daily from date due until remitted to fund

Statutory Landscape – Plan Contributions

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- Administrator: **must ensure all contributions paid when due**
  - Statutory standard of care under PBA
  - Common law standard of care (duty of loyalty and good faith)
- Scope of duty – not merely passive
  - Must make inquiries
  - Pursue delinquent employers
- If contribution not paid when due **administrator must notify Superintendent**
  - Applies only for single-employer plans.

Statutory Landscape – Plan Wind Up

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- Consequences of DB plan wind up:
  - All existing DB members cease DB accrual
  - All DB benefits are settled
  - Surplus crystallizes and must be distributed
    - Surplus uncommon for employers facing financial hardship
  - Deficit must be fully funded
  - DB plan and fund are terminated when all benefits have been settled
- DC plan wind ups don't have the same issues
  - No surplus/deficit

Statutory Landscape – Deemed Trust

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- PBA establishes **statutory deemed trust** with respect to contributions owing, but not yet remitted, to pension fund
  - Trust: protects contributions owing to plan from being seized/attached by other creditors of employer
    - Deemed trust applies to contributions not yet remitted to fund
    - Does not make fund itself, per se, impressed with trust

Statutory Landscape – Deemed Trust

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- Deemed Trust:
  - **operates** in ongoing plan and on wind-up
  - **applies** to money held by employer for employee contributions prior to deposit in fund, and to employer's contributions due but not yet paid
  - **applies** to interest accruing on employer and employee contributions owing but not yet remitted
  - **appears to apply** to funding deficiency on wind-up of plan to extent it relates to employer contributions and remittances due and owing to fund on wind-up not yet paid

Statutory Landscape – Deemed Trust

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- Limitations to application of deemed trust
  - Extends only to “**accrued**” contributions
  - **Does not exempt pension contributions** in hands of employer from being made available for distribution among employer’s creditors in **bankruptcy/insolvency** proceedings

Contributions During Employer Financial Hardship – Federal Relief

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- Federal Pension Benefits Standards Act (“PBSA”)
  - PBSA includes the concept of “distressed plan workout scheme”
  - Employer must certify as to its financial need for relief
  - Election will be followed by mandatory, finite negotiation period
  - During negotiation period, current service contributions must continue but other employer contributions will be deferred
    - Deferral will end and missed contributions will become due immediately on happening of certain events
  - Representative of plan beneficiaries to negotiate more definitive funding workout arrangement
  - Definitive funding relief must be approved by Minister of Finance and opposed by no more than one-third of beneficiaries

Key Cases

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- *Sun Indalex Finance LLC v. United Steelworkers*
  - Indalex commenced CCAA proceedings in April 2009
  - Two pension plans had a deficiency of $6.75 million
  - Sale transaction closed for substantially all of its assets
    - Debtor-in-possession lender could not be repaid in full
    - All other secured and unsecured creditors received nothing
  - Supreme Court of Canada (2013)
    - PBA deemed trust applies to entire wind up deficiency, HOWEVER,
    - DIP lender takes priority
  - Pension entitlements could be reduced by up to 50%

Key Cases

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- *Grant Forest Products Inc. v. Toronto-Dominion Bank*
  - Grant Forest entered CCAA protection in 2009, prior to DB pension plan winding-up
  - Company sold a number of assets
  - Ontario Court of Appeal (2015)
    - Deemed trust over the wind up deficiency did ***not*** attach to the company's assets because the plan had not been wound up at the time of the Initial Order under the CCAA
    - Takeaway: provincial provisions prevail prior to insolvency but not after
  - See also: Aveos Fleet Performance Inc. (federal PBSA); Timminco ltée (Quebec SPPA)

Recent Insolvency Proceedings

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- AbitibiBowater Inc. Insolvency
  - AbitibiBowater Inc. filed for CCAA protection in April 2009
  - Pension plan had an unfunded liability of ~$1 billion
  - Ontario and Quebec governments both agreed to provide restructuring support and funding relief
  - Pension payments to retirees continued; current employee wages cut
  - Target benefit plans were established for new employees and active employees on a going-forward basis
  - Abitibi emerged from CCAA protection in December 2010
    - According to 2012 financial filings, the pension liability under legacy pension plans has risen to $1.9 billion…

Recent Insolvency Proceedings

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- Auto Sector Collapse
  - Ford and General Motors both underwent restructurings
  - Offered lump-sum payment to current and/or former employees in satisfaction of pension entitlements
    - GM: also purchased a group annuity contract
  - Employees will elect how the payment is invested
  - GM Canada announced a plan to move to a DC model for salaried employees

Recent Insolvency Proceedings

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- Nortel Networks Insolvency
  - Insolvency proceedings commenced in January 2011
  - Effective September 30, 2010, Nortel ceased to make contributions to the plans
  - Unfunded pension liability of approximately $1.5 billion
  - Ontario Bill 173
    - Allows persons who are receiving a pension from the Nortel pension plans to have the value of their pension based on the plan funding ratio paid into a life income fund
    - Those who don't elect to transfer remain in the Nortel plans
    - Wind up process could continue until 2018 or beyond…

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