

## pensions and employee compensation bulletin

March 2009

### pension plans and liability in an uncertain economy: are directors and officers at risk?

The current economic situation has had a significant impact on the funding of registered pension plans. More defined benefit plans than ever are in deficit positions. Members in defined contribution plans have seen the value of their accounts decrease dramatically. Many members of both defined benefit and defined contribution plans are worried about their financial future and, in turn, are looking for answers. Can anyone be held accountable? Can anyone be blamed for the losses? What about the directors and officers of the organizations that sponsor pension plans? Are they at risk?

In this bulletin, we highlight some of the potential areas of risk for directors and officers who are involved in the sponsorship and administration of registered pension plans.

#### Overdue or Late Contributions

Faced with declining revenue and an uncertain economy, many employers are finding it increasingly difficult to make required contributions to their pension plans. Are directors and officers at risk if an organization fails to contribute to its' pension plan? In short, yes.

Under the Ontario *Pension Benefits Act* ("PBA"), an employer is required to contribute to the pension plan in accordance with the terms of the plan and the PBA. For a defined benefit plan, an employer's required contributions are the current service costs determined by the most recent actuarial valuation or the amount set out in a collective agreement. For a defined contribution plan, an employer's contributions are defined by the plan text and / or collective agreement. Failure to meet these obligations is an offence under the PBA and may result in the imposition of a fine against the employer. If the employer is incorporated, the directors and officers may also be at risk.

Under the PBA, a director, officer, official or agent of a corporation and every person acting in a similar capacity or performing similar functions in a unincorporated association is guilty of an offence under the PBA if he or she:

(i) causes, authorizes, permits, acquiesces or participates in the commission of an offence by the corporation or unincorporated association under the PBA or its Regulations; or (ii) fails to take all reasonable care in the circumstances to prevent the corporation or unincorporated association from committing an offence under the PBA or its Regulations. The penalty for such an offence, if convicted, is a fine of up to \$100,000 on first conviction and a fine of up to \$200,000 on subsequent conviction.<sup>1</sup>

In other words, if a corporate employer fails to contribute to the plan in accordance with the plan and the PBA, it commits an offence under the PBA and is subject to penalty. If the director or officer of that corporation authorized the missed contributions or did not take all reasonable care in the circumstances to prevent the missed contributions, he or she is also guilty of an offence under the PBA and is subject to penalty.

Over the past several months, we have seen a number of claims brought against directors and officers related to overdue or missed contributions to pension plans. Directors and officers need to be aware of the obligations of the plan sponsor under the PBA and the personal risks of non-compliance.

## Plan Funding and Plan Deficits

What if the employer has met all of its contribution obligations under the PBA? Can the directors or officers still be held accountable for deficits caused by plan funding decisions? In certain circumstances, yes.

An organization that sponsors and administers a registered pension plan wears “two hats”: the plan sponsor hat and the plan administrator hat. When it is acting as the plan sponsor, it may act in a self-interested manner. When it is acting as the plan administrator, it is considered a fiduciary and has a responsibility to act in the best interests of plan members and other beneficiaries. Claims for breach of fiduciary duty can be made against pension plan administrators in respect of a broad range of actions or inactions including: imprudent investment decisions; inequality of treatment between active members and former members; choice of service provider; funding decisions and choice of investment options.

As is highlighted in the decisions summarized below, when a pension plan is in a deficit position, claims against the parties seen to be responsible for the deficit may also follow.

In 2006, a group of former non-union members of a pension plan sponsored by St. Anne-Nackawic Pulp Co. applied for a court order appointing them as the representative committee for all non-union plan members with respect to the bankruptcy of the company and its underfunded pension plan.<sup>2</sup> In their application, the former members noted that a key issue was whether or not the directors of the company acted within legal authority in “creating the plan deficit.” The order was denied by the New Brunswick Court of

<sup>1</sup> Section 110

<sup>2</sup> *In the Matter of the Bankruptcy of St. Anne Nackawic Pulp Company Ltd. Pension Committee*, 2006 NBQB 31 (CanLII)

Queen's Bench for a variety of reasons, including that the applicants were represented by another party in the bankruptcy. In dismissing the order, the court did not comment on the role of the directors and officers, if any, in relation to the deficit. The order, if granted, would have given the former members access to all of the company's records.

In 2008, the Ontario Court of Appeal held that the actuaries being sued in connection with the deficits of two under funded pension plans could bring claims against the former directors, officers or employees of the plan sponsor and a related corporation.<sup>3</sup> The former directors, officers and employees were members of the Audit Committee. The Audit Committee decided how much money the plan sponsor would contribute to the pension plan each year.

The Court found that when the Audit Committee made decisions on the amount of contributions to the pension plan, it was acting as the plan administrator. As a result, the committee and its members, including the directors and officers, had a responsibility to act in the best interests of plan members. Although a court has not yet decided whether the directors and officers failed to act in the members' best interests, the case serves as a reminder of the duties imposed on pension plan administrators. When a director or officer is acting as the plan administrator, he or she has a responsibility to act in the best interests of plan members and beneficiaries.

## What can directors and officers do?

First and foremost, directors and officers of a corporation that sponsors a pension plan must understand their responsibilities under the plan. They must familiarize themselves with the PBA. They must, to the extent possible, know when they are acting on behalf of the plan sponsor and when they are acting as the plan administrator and tailor their actions accordingly. This is not an easy task as the line between the duties of a plan administrator and plan sponsor is not always clear.

Directors and officers who assist in the administration of the plan should review the indemnity provisions under the pension plan. They should also review the terms of the Directors' and Officers' liability insurance policy entered into by the organization. Is the insurance coverage broad enough to cover liability incurred as a result of a breach of fiduciary duty or the administration of a pension plan? In many cases it is not, and fiduciary liability insurance coverage may be required. While the risks of liability for a director or officer are likely greater in the current economy, there are steps that can be taken to minimize the risk.

3 *Morneau Sobeco Limited Partnership v. Aon Consulting Inc.* (2008), 65 C.C.P.B. 293 (Ont. C.A.)

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**a cautionary note**

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