RESPONSE TO THE CONSULTATION DOCUMENT

ENHANCING RETIREMENT SECURITY FOR CANADIANS

December 21, 2018

Canadian Federation of Pensioners

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Table of Contents

1. **Overview** 1
   (a) Benefits reinvested into the economy 2
   (b) Putting DB Plan history in context 3
   (c) Critical examination of corporate behaviour 6
   (d) Specific examples of corporate misdeeds and attempted misdeeds 8
      (i) Sears 8
      (ii) Indalex 8
      (iii) VON Canada 11
   (e) Attacks on Existing Protections at the Provincial Level 12
   (f) Overestimating the scope of the solvency problem 13
2. Responses to the Consultation's Proposals 13
   (a) Amending Solvency Legislation 13
   (b) Solvency Reserve Accounts (SRAs) 17
   (c) Pension Funding Relief Criteria 17
   (d) Transfers to self-managed accounts 18
   (e) Clarify benefit entitlement 18
   (f) Restrictions on corporate behavior 19
   (g) Increased reporting and disclosure requirements 19
   (h) Enhance look-back period 20
   (i) Enhanced transparency in the CCAA process 20
3. CFP/NPF Proposals not contained in the Consultation Paper 22
   (a) Backstop 22
   (b) Pension Insurance 22
4. Summary and conclusion 22

1. **Overview**

The Canadian Federation of Pensioners (CFP) is pleased to provide its comments regarding the federal government's consultation *Enhancing Retirement Security for Canadians*. CFP is an organization dedicated to improving the security of defined benefit (DB) pension plans in Canada. Each of CFP's twenty member organizations advocate for the interests of the active and retired members of workplace DB pension plans. Collectively, the CFP member organizations represent the interests of more than 250,000 individuals and their families across Canada.

CFP's position has always been that pensions are deferred wages, a commitment made over decades by employers, with only government legislation to protect them. Pensioners should receive their full pensions.

The National Pensioners Federation (NPF) also joins CFP in supporting this submission. The NPF is a national, not-for-profit, non-partisan, non-sectarian organization of 350 seniors chapters, clubs, groups, organizations and individual supporters across Canada with a collective membership of 1,000,000 seniors and retirees devoted entirely to the welfare and best interests of ageing Canadians. NPF's goal is to ensure seniors and retirees have a life of dignity, independence and financial security. The NPF and all of its affiliates recognize the importance of standing up in a clear, unified, national voice for the success of sound government policy and legislation. It is NPF's intent to persist in this work with the CFP and NPF's partner organizations to achieve protected and secured defined pension plans for all Canadians.

CFP and NPF believe that increasing pension security should involve a number of measures.

Extending super-priority to the unfunded pension liability is one measure that is, in the CFP and NPF view, the most practical solution as it is entirely within the federal government's ability to implement and can be done within the regime of legislative changes in their control.

We are encouraged by the government's examination of options to enhance retirement security. However, we believe that other options, beyond the specific ones laid out in the paper, should also be considered. Canada's pension security regime lags behind that of other of our major trading partners when viewed as a whole. For example, other countries such as the US and UK have guaranty or insurance funds to protect against pension shortfalls. In CFP's view, implementation of such fund that protects all earned pension amounts should be a priority in Canada and would be the most effective means of addressing pension security. Moreover, a fully funded guaranty fund can be implemented at no cost to taxpayers and at a very small cost to employers. In fact, in Canada, Ontario has such a plan, funded at no cost to the taxpayer (though in our view, Ontario's fund is in need of improvement to increase the coverage levels). Employers who criticize solvency requirements argue that such requirements, in effect, require every employer to insure its pension plan against the employer's own business failure, which failures are rare events in practice. A guaranty fund, on the other hand, allows employers to pool and share the risk of these rare events amongst a large group, thereby lowering the cost to everyone. Implementation of a guaranty fund can thus represent a win-win situation for employers and pensioners. With the implementation of a guaranty fund, many of the other issues

associated with pension security become moot. We therefore urge the government to take steps to implement such a fund for federally regulated pension plans and as a best practice example for other provinces.

There are a number of measures the federal government could enact. It is critical that combined these measures result in pensioners receiving their full pension as promised. To ensure full pensions are received we propose a backstop be implemented. The backstop would take the form of a recurring annual refundable tax credit equal to the amount of pension lost by an individual due to insolvency. If measures implemented arising from this consultation result in pensions paid in full by the companies and the commercial interests around them, the tax credit would be zero. There would be no cost to the government and this is CFP's preferred option. If, however, the government chooses not to place the full burden on companies for the commitment they have made to pensioners, the tax credit would be a means to partially assist the pensioner as he or she seeks to supplement pension income from other sources. It would be partial because its full effect depends on a number of factors including the marginal tax rate of that taxpayer and the resulting after-tax impact of the credit. It nevertheless would be a valuable backstop.

That said some of the other measures, bought forward in the consultation document, could be implemented to increase the protection afforded by super-priority and a federal pension insurance program.

We will provide our views on some of them below.

Prior to dealing with the specific proposals presented in the Consultation Paper, it is useful both to understand the history of the defined benefit pension plan in the Canadian context factoring in a number of the external influences that have led us to where we are today and to appreciate the economic benefits of ensuring stability and security in the defined benefit plan system. To be clear, CFP is an advocate for defined benefit pension plans. The pooling of longevity and investment risk enables these plans, when properly designed and funded, to meet the needs of Plan members throughout their retirement and allow plan retirees to continue to contribute to the economic stability and growth of the Canadian economy.

(a) Benefits reinvested into the economy

Whenever the topic of providing priority and protection for pension plan benefits is put on the table, there is a hue and cry from the financial services sector that such protections will dampen the ability to efficiently deal with business restructuring and business financing. Seldom is there discussion of the economic harm done when promised pension benefits are not preserved.

Several of the major jointly-sponsored pension plans in Ontario commissioned a study by the Boston Consulting Group. One of the purposes of that study was to analyse the economic impact of retired members' spending. BCG concluded the following,

> The benefits paid out to DB pension plan members ultimately flow back into the Canadian economy in the form of consumer spending and taxes, generating business growth and employment, and generating revenues for all levels of

> government. Using the reference years 2011 and 2012, it is estimated that beneficiaries spend **$56-63 billion** annually on consumable goods, shelter, durable goods, recreation, services, and sales and property taxes. They pay an additional **$7-9 billion** in income taxes, while a further **$2-3 billion** flows back into their savings. Payouts of DB plan benefits to members are reinvested in the Canadian economy through various channels. [emphasis added]
>
> Annual spending by DB plan beneficiaries on durable and consumable goods is estimated at $56-63 billion and is widespread across the economic spectrum.
>
> Canada's senior population continues to be a significant source of revenue for all levels of government throughout their retirement years. For those who are the beneficiaries of DB pension plans, total taxes paid are estimated at $14-16 billion annually. The breakdown is about $7-9 billion in income tax, $4 billion in sales tax and $3 billion in property tax.[1]

The same BCG study asked the question "What would be the impact on the Ontario economy if there were no defined benefit pension plans." It concluded that income sourced from defined benefit plans increased consumable spending by 75%, shelter by 100%, durables by 66%, recreation by 150% and services by 300%.

When addressing retirement security issues, it is incumbent on the government not only to attend to the submissions of Bay Street advocates but to recognize that the ongoing investment made utilizing DB plan assets and the spending by retirees facilitated from DB proceeds are fundamental factors that must be weighed when balancing the interests of the various stakeholders. This becomes increasingly important as the portion of the Canadian population over age 65 continues to rise.

(b) Putting DB Plan history in context

The development of defined benefit pension plans was shaped by the administrative and regulatory requirements first imposed federally through income tax legislation and accompanying administrative guidelines and, subsequently, from the mid-1960's onward through the combination of minimum standards pension plan regulation provincially and federally and the overlay of income tax requirements.

Since 1919, income tax legislation gradually gave special consideration to pension plans. In that year a section added to the Act exempted from income tax any amounts deducted by the employer from the employee's wages in connection with pension funds. The first provision

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[1] Information is sourced from a Study conducted by The Boston Consulting Group (BCG) and commissioned by Healthcare of Ontario Pension Plan (HOOPP), Ontario Municipal Employees Retirement System (OMERS), OPSEU Pension Trust (OPTrust) and Ontario Teachers' Pension Plan (OTPP). The materials excerpted by commissioners from the Study referenced were provided for discussion purposes at the 2013 Lancaster Pension Conference and was not intended to be relied on as a stand-alone document. Additional analysis was done to the data and analysis contained within the Study by third parties other than BCG. BCG did not independently verify this additional analysis and assumes no responsibility or liability for it.

exempting employer contributions to a pension fund came in 1938, in respect of employer payments into a pension fund for an employee's past services. Deductions for employer contributions for future services were first allowed in 1941.

There was already a developing tradition of employer pension plan provision prior to the introduction of sections into the Income War Tax Act. By 1900 a number of large companies had established pension plans and there was a tradition of government superannuation since 1870. Employers followed an English court decision that ruled contributions to pension plans could be categorized as a deductible general business expense under British tax law (*Atherton* v. *British Insulated and Helsby Cables Limited,* (1925) 10 T.C. 155; *C.I.R.* v. *Bell,* (1927) 12 T.C. 1181). Consequently, analysts did not see the need for specific legislative provisions governing the deductibility of employer current service contributions under the IWTA and subsequent versions of the ITA. Past service contributions were another matter. Since a past service contribution could not be related to the current service of an employee, it could be challenged as an ineligible expense. The 1938 provision was therefore welcome in that it provided explicit authority for the deduction of employer past service contributions.

The motivation of the Department of Finance and the Department of National Revenue during the 1940's was less pension promotion and more to protect against loss of fiscal revenue. During and shortly after World War II, Canada imposed an excess profits tax on 100 percent of profits in excess of a pre-war base. Corporations were tempted to pay large sums into pension plans as a means of avoiding tax liability since such contributions were not subject to the same tax treatment as salaries then were. In response, the DNR introduced rules that required that special payments into pension plans be certified by an actuary and deductions amortized over ten years. In addition, any contributions by an employer in respect of past service had to be irrevocable. If the plan were ever to be wound-up, it was a condition of pension plan approval that the surplus be distributed to plan members in the form of enhanced benefits. In John Forsyth's address to DNR staff at a DNR conference in 1949 he alluded to the potential problems that might ensue for plans that provided benefits to major shareholders and the possibility of manipulation of wage scales to provide enhanced benefits to business owners. This would eventually lead to restrictions on pension plans covering shareholders.

The first time the concept of an "approved fund or plan" was introduced to the IWTA was in 1942. Employers were required to obtain approval from DNR for their pension plan. The Act did not specify the minimum requirements to be met in order to obtain approval or a procedure to authorize the enactment of such rules. Despite the apparent lack of legal authority, the DNR first published principles and rules respecting pension plans and procedural requirements for approval in 1947. These principles and rules (commonly referred to as the "Blue Book") were a mix of minimum pension standards (now typically associated with provincial pension standards legislation), application procedures and mandatory pension provision requirements such as the irrevocability of employer pension contributions. Legal analysts at the time suggested that the social nature of some of the principles and rules went beyond fiscal policy and was likely a breach of constitutional jurisdictional authority. The rules were never made the subject of a constitutional challenge. However, the 1959 release of Information Bulletin No. 14, the successor to a series of Blue Books, saw the deletion of most of what could be termed social-based requirements. By the mid-sixties, with the introduction of provincial pension plan

minimum standards legislation, provincial registration became a condition precedent to registration at the DNR.

The Blue Books and subsequent policy directives had a significant impact on the drafting of plan and trust terms. Most plans drafted in the 50's, 60's and 70's contained provisions designed to ensure that pension funds were used for the benefit of employees. Most documents did not even address the issue of plan surpluses but, if addressed, surplus was typically assigned to the plan members. The high interest rates of the 1970's led to accumulation of significant surpluses in existing pension plans. The federal government did an about face effective January, 1982 by shifting from the irrevocability of contributions to imposing specific limits on the amounts that could be accumulated within the pension fund. Surplus funds that accumulated above a specified limit were mandated to be returned to the employer. As a result, new plans typically inserted a provision providing for the reversion of surplus to the employer and many existing plans were amended to reflect the new rules thereby transferring surplus rights from plan members to the employer.

The 1980's marked a turning point for defined benefit plans for a number of reasons. With most DB plans healthily in the black, actuarial consulting firms prospered. For example, William M. Mercer Limited, then the industry leader in Canadian pension consulting firms was growing at a rate of 20% per year. With ample assets available to pay plan expenses, for many plans, expense controls were not a focus. However, that was soon to change. Ontario went through a major pension regulatory reform that incorporated new funding requirements in the mid-80's applicable from 1987 onward. Concurrently, the federal government initiated a wholesale review of the income tax policies applied to retirement savings and pension plan provision. Effective in 1989, applicable for existing plans after a transition period to 1992, an integrated and exceedingly more complicated system applied to an array of deferred plans including registered retirement savings plans, defined contribution plans, deferred profit-sharing plans and defined benefit plans.

The increased complexity led to a significant amount of consulting dollars being spent by plan administrators to understand their new requirements. Several factors provided incentives for executives to examine the viability of either winding up DB plans or converting from a defined benefit to a defined contribution design. The North American Free Trade Agreement and the break-up of the Soviet Union both promoted looking toward globalization of business activities. There was a push, particularly on the part of the U.S. government, to eliminate barriers to business in new markets by minimizing the impact of labour and employment laws in other countries while promoting access to businesses and resources at the lowest cost possible. That message was also incorporated into domestic human resource practices. Outsourcing and moves away from full time employment and the associated benefit costs became an ingrained strategy. The 1991 recession prompted CFO's to sharpen their pencils and look for available sources of financing and cost control within their organizations. CFO's took note of the excessive expenses being charge to their defined benefit plans. More importantly, the change in the approach to surplus ownership by the federal government and the resulting amendments to plan terms incorporating those changes provided the perfect combination for some employers to develop approaches that would allow access to surpluses in existing plans. At the very least, contribution holidays were taken. At the worst, plans were collapsed so that surplus could be brought back into mainstream business revenues. But the taking of contribution holidays and the use of surplus

assets were to become hotly contested issues prompting a significant amount of costly litigation and uncertainty. Despite the demonstrable long-term benefits associated with the defined benefit plan model, many plan sponsors sought to exit the system. And the benefits consulting community jumped in full throttle to assist by promoting plan conversion models as part of their annual plan design reviews.

Many plans that were in existence in the 1980's and continue today are underfunded but also have an extensive history of taking contribution holidays. In one example, a DB plan took contribution holidays for 17 consecutive years in the 1985 to 2002 period. The total amount of contributions avoided even without factoring in the lost investment income on contributions that would have been gained had the contributions been made equaled the total current deficit on a solvency basis. The requirement to cease contributing when there is excess surplus works to make the contribution cycle more volatile. There is a 25% likelihood that a 10% actuarial surplus in a plan valued on a going-concern basis and with assets smoothed will evaporate over any three year valuation cycle.[2] A larger funding buffer can make pension contributions more predictable by reducing the need to increase pension contributions when there is an economic downturn or market correction—exactly when many employers are looking to reduce costs. While the federal government responded to this concern in 2010 by raising the excess surplus limit to 25% for contributions made to plans in respect of post-2009 service, it is questionable whether there is any need for a surplus cap. Employers are highly unlikely to over-contribute to pension plans, particularly given the corporate behaviour discussed in the following sections.

The new millennium did not slow the decline in private sector DB plan representation. The dot.com crash followed by the 2007-2008 financial debacle had significant effect on the perceived viability of the DB model. The mobility of the labour force argued against a single employer design. Low interest rates increased solvency funding requirements. The extended term and the continued decline of interest rates led to considerable volatility in funding requirements and generally meant that most DB plans were underfunded on a solvency basis for an extended period. This prompted more plan sponsors to close plans to new members if not to terminate plans altogether. DB plans continued to be the target of defined contribution advocates, some going as far as labelling DB plans ponzi schemes. Many in the pension benefits industry have now concluded that the DB structure is not viable despite the success of the jointly-sponsored DB pension plan model and the continued existence of private sector DB plans providing retirement benefits to approximately two million retirees.

Unfortunately, the dialogue all too often has focused on the conditions of the day rather than focusing on the long-term pension horizon. Conclusions have often failed to factor in significant anomalies and biases in corporate behavior, poor policy choices on the part of pension plan regulators, imbalances in the solvency regime and an assumption that the funding and solvency issues are worse than the data indicates. The following section speaks to the corporate behaviour issue in greater detail.

(c) Critical examination of corporate behaviour

[2] Pierlot, James and Bonnar, Steve, *A Tale of Two Tax Rules,* Benefits Canada, October 2007.

Everyone is acutely aware of the widening gap between the compensation levels of senior management and executives relative to the corporate workforce. Unfortunately, the incentives in place to assess and reward executives are unduly short term in nature and provide the stimulus to make suboptimal decisions for the company and its employees.

In a study by John Graham, Campbell Harvey and Shiva Rajgopal, 400 CFOs of large U.S. public companies were asked about their decision-making priorities. 80% of them said that they would sacrifice economic value for the firm in order to meet the quarter's earnings expectations. Two other studies focused on share buybacks demonstrating that a disproportionate share of their earnings is used to repurchase their own stock rather than investing in future growth. A University of Illinois study showed that a large share of buybacks occurs when a corporation would miss its earnings target were it not for the buyback. The executives cite capital markets as placing unrealistic and unproductive constraints on them.[3] It is difficult to empathize when there is no hesitation in accepting the compensation bonuses associated with meeting these targets.

The short-termism problem is not abating. If anything, it may be getting worse. A 2014 global survey of more than 600 C-suite executives and directors, conducted by the non-profit Focusing Capital for the Long Term (FCLT), reported that two-thirds of those surveyed said pressure for short-term results had increased over the previous five years.[4] Yet, the evidence is clear that those who do adopt a long-term view actually provide greater rewards to shareholders in the long-term. Companies that spent on average 50% more on R & D, cumulatively grew on average 47% more than that of other firms, and with less volatility. Cumulatively, the earnings of long-term firms also grew 36% more on average.

The short-termism carries over and has implications for DB pension funds. The Canadian Centre for Policy Alternatives examination of pension deficits and shareholder payments revealed that Canada's largest companies paid out four times more to shareholders than it would have cost to fully fund their pension plans. The study examined the 39 companies on the S&P/TSX 60 that have DB plans. The aggregate deficit of those plans in 2016 was 10.8 billion dollars. Yet, shareholder payouts in 2016 amounted to $46.9 billion. Those pensions described as in the worst shape with shortfalls under 80% could be fully funded with only 6% of the shareholder payments since 2012. The study concluded that almost all DB plan shortfalls could be rapidly eliminated with little impact on shareholder payments.[5]

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[3] Martin, Roger L., *Yes, Short-Termism Really is a Problem,* Harvard Business Review, October 9, 2015, (https://hbr.org/2015/10/yes-short-termism-really-is-a-problem)

[44] Carey, Dennis; Dumaine, Brian; Useem, Michael; and Zemmel, Rodney, *Why CEOs Should Push Back Against Short-Termism*, Harvard Business Review, May 31, 2018 (https://hbr.org/2018/05/why-ceos-should-push-back-against-short-termism)

[5] Eisen, Cole; Macdonald, David; and Roberts, Chris, *The Lion's Share: Pension deficits and shareholder payments among Canada's largest companies*, Canadian Centre for Policy Alternatives, November 2017

(d) Specific examples of corporate misdeeds and attempted misdeeds

(i) Sears

The Sears Pension Plan was left with a $267 million funding shortfall on a wind-up basis when Sears shut its Canadian doors. Since 2010, Sears paid to shareholders through dividends and share buybacks $1.5 billion. Shareholders received 5.5 times the amount it would have taken to eliminate the pension deficit in its entirety. The Sears example begs the question "what restrictions should be placed on corporate executives with respect to shareholder payouts and buybacks given their pension funding obligations?".

(ii) Indalex

Indalex manufactured aluminum extrusions. In 2006, it was the second largest supplier in the market and had, at the time it was purchased by a U.S. private equity firm (Sun Capital) in 2006, twelve plants, eleven operating in North America, one in Hong Kong. This is one of those stories where a private equity firm sees an asset rich company and believes it can make a healthy profit in short order by orchestrating a highly leveraged buyout. Sun Capital set as a goal making a $50 to $60 million dollar premium in three years or less (approximately a 52% ROI).

In 2006, Indalex had an asset to debt ratio of three to one and was profitable. Sun Capital, through its affiliates, orchestrated a buyout that increased Indalex's debt, bringing the ratio down to one to one. The terms of the purchase introduced a requirement to pay management fees to Sun Capital affiliates and a commission on any financing transactions. It was also clearly the intent of Sun Capital to sell certain of Indalex's assets to facilitate recovery of the purchase costs through the issuance of dividends in short order.

Sun Capital did not anticipate the financial market collapse of 2007/2008. Since Indalex supplied a significant amount of its product to the construction sector, it naturally suffered a depression in sales as financial markets deteriorated. By the end of the first quarter of 2007, Indalex had seen a year over year decline in sales of 62%. Indalex increased its use of cash by over 400% in 2007. The CEO, as part of its Form 10-K filing with the Securities and Exchange Commission (SEC) stated publicly that there would be no dividends declared in the foreseeable future. At the same time, Indalex had retained FTI Consulting to prepare a solvency report to justify the payment of 76 million dollars in dividends to Sun Capital affiliates. In fact, it threatened to fire FTI as its accountant if it did not issue a favourable solvency opinion.

In violation of the public announcement, prudent management of the firm and conflict of interest standards, the Board of Directors authorized the dividend payment (which, incidentally, also meant that each Board member would receive dividend payments as shareholders in Indalex). Add to this over ten million dollars in management fees paid to Sun Capital affiliates and the total outpouring in 2007 was over 86 million dollars. By mid-2008, Sun Capital had recovered 85% of its investment in Indalex, despite the financial market collapse and its effect on Indalex sales. The details of these transactions were not on the Court record in the Canadian *Companies*

Creditors Arrangement Act (CCAA) court proceeding and therefore did not influence the determination made at the Superior Court, Ontario Court of Appeal and the Supreme Court of Canada.

In March and April of 2009, Indalex entered into Chapter 11 bankruptcy proceedings in the United States and *Companies Creditors Arrangement Act* (CCAA) proceedings in Canada respectively. As part of the US proceeding, a senior consultant at FTI Consulting was appointed as the Chief Restructuring Officer (CRO). This is a management position. In effect, the CRO worked hand in hand with the Indalex CEO and Board to assist in the development of a restructuring plan.

In the CCAA proceeding, the Canadian subsidiary of FTI was appointed as the Monitor. The Monitor acts as an officer of the Court assisting the Court in assessing the status of the debtor company, the restructuring proposals, the creditor claims, etc. It is fundamental to the workings of the CCAA process that the Monitor be independent of the debtor company. Unfortunately, there was an apparent conflict of interest built into this appointment since FTI also acted as the CRO and had (unbeknownst to the Court) also prepared the solvency report used to justify the 2007 dividend payout.

There were two registered pension plans tied to Canadian Indalex operations. One was an executive plan. It had not been wound up at the time of the CCAA proceeding. It had a deficit of approximately 3.2 million dollars. The other plan was a salaried plan that covered both non-union and some union Indalex personnel. While the salaried plan had been wound up, it had a deficit of approximately 1.79 million dollars at the time of the CCAA filing.

Early in the CCAA proceeding a debtor-in-possession (DIP) loan was negotiated to fund ongoing operations during the restructuring. The loan was slightly under 28 million dollars and was guaranteed by Indalex US and by Sun Indalex, an affiliate of Sun Capital and the entity which indirectly owned 100% of the voting shares in Indalex. That financing only occurred because the Unsecured Creditors Committee in the United States threatened to sue Sun Indalex unless it provided the cash injection in light of the facts outlined above. This loan was granted priority over the claims of creditors in the CCAA proceeding without providing notice to pension plan members. When all assets of Indalex were sold, there was a shortfall of 10 million dollars in respect of the DIP loan repayment. Indalex US advanced the ten million dollars to satisfy the shortfall.

At the time the sale was approved, counsel representing both registered plans claimed that the pension deficits should take priority over other claims, including the DIP loan claim. The pension claims were based on the Pension Benefits Act protections termed “deemed trusts”. Counsel argued that the PBA provided a superpriority covering the whole of the pension deficits and that, as a result, the pension deficits should be paid prior to distribution of the sale proceeds. The CCAA Judge approved the sale and distribution of the assets but set 6.75 million dollars on reserve pending consideration of the pension claims.

On the motion before the CCAA Judge, counsel for Indalex sought leave to place Indalex in bankruptcy, a step that would defeat the PBA claim. The CCAA Judge declined to permit the

filing for bankruptcy[6] but ruled that the PBA protections did not apply since the amount payable under the salaried plan was not due at the time of the sale and the protections of the PBA did not cover the executive plan since it was not wound up.

The CCAA decision was appealed to the Ontario Court of Appeal. There were a number of issues argued at appeal. First, no notice was provided to the pension plan members before the DIP loan priority was established. Second, Sun Indalex, who claimed the amount on reserve as a result of the DIP loan guarantee, was a related party. Indalex had an obligation to defend the interests of pension plan members since it was the plan administrator. Instead it took all steps to defeat the pension plan claims and support the Sun Indalex claim, arguably in breach of its fiduciary duties. Finally, it was argued that the PBA provisions covered the whole of the wind-up deficit and could not be defeated by the CCAA unless evidence was put forth demonstrating a clear conflict between the CCAA and the PBA. Since no evidence had been offered during the CCAA proceeding, the PBA claim should be enforced.

The Court of Appeal decision supported all aspects of the Plan member arguments. It found that no evidence had been put before the CCAA Court to override the PBA requirements. It ruled that the PBA deemed trust covered the entire Salaried Plan deficit and that payout of that deficit takes priority over the Sun Indalex claim. For the executive plan, because it was not wound up at the time of the CCAA proceeding, the Court relied on a finding of breach of fiduciary duty to order the payment of the executive plan deficit.[7]

The success at the Court of Appeal centered on procedural breaches by Indalex (lack of notice to Plan members), conflicts of interest amongst FTI and Indalex which led to decisions supporting related parties instead of Plan members (breach of fiduciary duty), a failure to present evidence of conflict between the CCAA and the PBA, and a determination that the scope of the deemed trust supported priority payment of the entire deficit.

The Court of Appeal decision stoked a firestorm. Representatives of the business and financial services community banded together to orchestrate the publishing of numerous articles claiming that the decision would cause havoc on the credit markets, render debtor in possession financing impossible to obtain or, alternatively, inordinately expensive thereby leading to the windup of companies as opposed to their restructuring.

Leave to appeal to the Supreme Court of Canada was sought and obtained. A selection of the articles referred to above were included in the submissions of the appealing parties and intervenors that challenged the Court of Appeal decision. Organizations such as the Canadian Association of Insolvency and Restructuring Professionals and the Canadian Bankers Association joined together with the appellants to assert that the Court of Appeal decision would have a devastating effect on credit markets and the efficiency and viability of restructuring. CAIRP challenged that imposing a notice requirement to Plan members and retirees prior to establishing superpriorities for administrative charges and DIP loans was untenable and could, in an of itself frustrate the restructuring process. It went as far as to suggest that a notice

[6] Technically, what was sought was leave to lift the CCAA stay to permit a voluntary assignment in bankruptcy.
[7] The Court concluded that the deficit was covered by a constructive trust which took priority over the DIP claim.

requirement would place plan members in an advantaged position relative to other creditors thereby undermining the equity in the system.

The Canadian Bankers Association asserted that the Court of Appeal decision injected great uncertainty into the business of bank lending both for healthy and distressed companies with defined benefit plans and that it would affect the price and availability of credit. Despite these assertions, the evidence showed that distressed companies that entered into the CCAA process after the issuance of the Court of Appeal decision and before the rendering of the Supreme Court of Canada decision were able to obtain DIP loans and at comparable rates to that obtained prior to the Court of Appeal decision. From the CFP perspective, the assertions made by these interveners were based on conjecture as opposed to fact and, as will be discussed in the next section, the incidence rate and quantum of plan failures in Ontario, the jurisdiction with the most private sector defined benefit plans, has been year over year relatively small in comparison to the total asset base of defined benefit plans. The objective data does not support the supposition that bringing Plan members and retirees into the insolvency process early and with priority rights would undermine credit markets.

The Supreme Court rendered a long and complex decision on the Indalex issues. The majority concluded that the deemed trust applies to the full windup liability of a pension plan. But, DIP financing will override the deemed trust if given priority in the court order. Indalex had failed to meet its fiduciary duty to plan members when it did not provide notice to them prior to establishing the DIP priority and as it related to conflicts of interest exposed during the proceeding. But, for a distressed pension plan that was not wound up at the time of entering the CCAA proceeding, there was no relief as the Court refused to impose a constructive trust over the Indalex assets so that these plan liabilities could be satisfied.

While the SCC decision forced players in subsequent CCAA and bankruptcy proceedings to be cognizant of the plan members and retirees and to seek their input earlier in the proceeding, the decision was essentially a glass half full. Restructurings are orchestrated by the management of distressed companies usually in consultation with restructuring professionals. It is a closed network and information as to the details are revealed only at the 11th hour. Those who have often dedicated their working lives in the service of a company are excluded from the process until the deals have been done. In the absence of formal protection in the form of a superpriority for pension claims, the plan members are treated as mere unsecured creditors on the same footing as a supplier that has supplied products or services over the short-term. There is no recognition of the difference in the magnitude of the commitment made to these Plan members relative to external service and product suppliers and short-term lenders who have unsecured claims.

(iii) VON Canada

The importance of early participation by representatives working on behalf of plan members can be exemplified in the CCAA VON Canada proceeding. In that proceeding, VON Canada was attempting to restructure. A decision was made to shut down certain VON operations. VON Nova Scotia and VON Ontario would continue under the VON Canada banner while VON West would be shut down. Representatives of VON Canada management and the Chief Restructuring Officer indicated that they would be seeking authorization to reduce VON West Plan member

benefits in accordance with the current solvency ratio of the VON Canada Plan. In effect, the intent was to treat the terminations as a partial plan windup. Of course, the fundamental flaw in this approach was that there is no legal basis under the AEPPA nor under the Ontario *Pension Benefits Act* to effect a partial plan wind-up. Neither jurisdiction contemplates partial plan terminations. In the absence of partial plan terminations, group terminations as a result of a restructuring are treated no different from individual terminations.

The United Nurses of Alberta ("UNA") stepped in to advocate on behalf of the Plan members who would have suffered permanent benefit reductions had the plan moved forward.

Each of the regional entities had separate boards of directors, but there was no independence in their governance. The President and Chief Executive Office of VON Canada swore an affidavit in support of VON's CCAA application. In that Affidavit, she stated:

> 12 … VON Canada and the Regional Entities operate as an affiliated corporate group. Operationally, VON Canada is fully integrated with each of the Regional Entities. Each Regional Entity has a board of directors <u>composed of the same individuals who comprise the VON Canada board</u>. The members of each Regional Entity are VON Canada itself as well as the individual VON Canada directors. VON Canada's senior management team is also the senior management team of each of the Regional Entities. [emphasis added]

Essentially, there was no independent governance of VON West. VON Nova Scotia and VON Ontario sought to avoid having to fund the shortfall for these terminated VON West employees. Were it not for the intervention of UNA, that is precisely what is likely to have happened despite the questionable legal basis upon which the benefit reductions would have taken place.

Independent representation on behalf of retirees and pension plan members is vital to defending their interests. In the VON Canada example, UNA was able to interject before the implementation of the benefit reductions could take place. The longer the period of time before involving that representation, the less likely it is that alternative solutions can be found.

(e) Attacks on Existing Protections at the Provincial Level

In the absence of federal reforms to the BIA and the CCAA to accord superpriority to pension claims, reliance has been placed to the extent possible on provincial deemed trust provisions. Given the constitutional division of powers, the deemed trust priority can be skirted by entering into bankruptcy or through establishing, as in Indalex, DIP financing and administrative charges that rank above any deemed trust priority. The previous Liberal government in Ontario had established a Business Law Advisory Council. In a Fall 2016 report, it recommended adjusting the deemed trust priority in Ontario so that collateral for derivatives contracts would rank above pensioner claims. The proposal put forward was characterized as a compromise to meet the interests of pension advocates.

In fact, the proposal was in no way a compromise, it was a proposed take away. Advocates for the proposal focused on BIA proceedings and suggested that, given the ineffectiveness of

deemed trusts in bankruptcy, the changes would be of no consequence. However, opponents to the proposal emphasized the influence that deemed trusts can have in CCAA proceedings and generally with respect to a pension plan sponsor's compliance with pension contribution obligations. In instances where there is not a liquidation, the subsection 30(7) provision under the provincial *Personal Property Security Act* does provide some leverage, particularly post-Indalex, to engage in negotiations on pension matters. Moreover, the issue of properly informing pension beneficiaries and ensuring that sufficient information is provided to them early in the CCAA process was an outcome of the Indalex proceeding. The two issues are not unrelated as there is then an ability on the part of representatives of pension beneficiaries to engage and advocate on their behalf. The assumption that subsection 30(7) affords no protection and therefore it is a non-issue to strip away the pension plans' priority was inaccurate. The "compromise" was only a compromise between a proposal that would ignore pension plan priorities in total and one that attempts to carve out a derivative priority and preserve the pension plan priority as a lower ranking priority.

The dialogue at the provincial level points to the need for a national solution embedded in the BIA and CCAA. Application of deemed trust provisions is uneven at best and, as noted above, of no effect in BIA proceedings. The financial services sector continues to seek ways to minimize the effect of the Indalex decision. As opposed to bolstering plan member protections, proposals such as that referred to above, would have the opposite effect.

(f) Overestimating the scope of the solvency problem

Policy decisions should be based on substantiated facts, not suppositions. Every time the notion of providing greater protection to pension plan members and retirees through insolvency legislation reforms has been raised, the financial services community has presented a doomsday scenario positing that providing priority for pension claims would undermine restructuring initiatives and be an overall detriment to the economy. These statements beg the question what would be the total hit if priorities were granted to these claims.

The Financial Services Commission of Ontario provided data to the CFP on defined benefit pension plan windups from 1982 through 2014. In total, there were 225 plan windups that resulted in deficits. The total windup deficit across all plans in deficit for all years amounted to slightly over $3 billion dollars. While that sounds like a significant amount, averaged over the 32-year period, this amounts to an annual deficit of under $100 million. Contrast this with the economic benefit of having defined benefit plan commitments honoured. The BCG study concluded that income from defined benefit plans in Ontario is used to spend $3 billion on consumables by retirees, $3 billion on shelter, $2 billion on durables, $3 billion on recreation and $3 billion on services. The data shows that the average unfunded liability for wound up plans over the last 32 years was $96.5 million per year. The economic benefit of protecting these pensions would appear to far exceed the financial impact of providing priority funding for these deficits.

2. Responses to the Consultation's Proposals

(a) Amending Solvency Legislation

There is asymmetry of information inherent in the insolvency system. While no one insolvency shares all of the same facts as another, it is often the case that restructuring initiatives are the subject of detailed planning for months prior to an application being filed, typically in a CCAA proceeding. The major players in the insolvency industry know each other, sometimes representing the company, the monitor, the trustee or major secured creditors and they share similar views as to who should have a say and when in resolving matters in a distressed company. Interests of unsecured creditors, on their terms including pension plan members, generally are not on the table. As plans are developed, employees, pension plan members and retirees are on the outside looking in. Prior to the Indalex appeal, it was often the case that the major deals had been struck and approved by the Court before representatives of employees and plan members had any detailed knowledge of the implications and often were not even notified of the motions seeking court ratification of such actions. The United Steelworkers, representing members in the salaried plan were provided with notice of the CCAA proceeding the night before the initial hearing date in the Indalex case. The executive plan members were not notified prior to the issuance of the Initial Order. Yet, when plan members have sought redress in CCAA proceedings, judges have often voiced the opinion that the court orders issued were public knowledge and the time had passed to object to these past court orders even when these orders struck down pension priorities, sometimes suspended current contributory obligations and would have the effect of permanently underfunding the pension promise.

The CFP does not dispute that it is necessary to plan a restructuring without broad dissemination of the details of the restructuring plan while it is being developed. Public knowledge that a company is considering an insolvency proceeding can exacerbate an already difficult situation possibly prompting a run on the shares of a publicly traded company and the withdrawal of the services of key suppliers. While it is generally agreed that the planning stage cannot involve a broad-based communication requirement, the issue is how that plan is dealt with once the CCAA proceeding is commenced, what role representatives of pension plan members and retirees should be given and what priority should be placed on pension benefit claims.

The Indalex case presented a classic example where management actively worked to undermine the claims of the plan members and retirees. The company had no intention of honouring the shortfall in funding of the Executive Plan, but it took no steps to windup the plan. The reason was obvious. If the plan was wound up prior to applying under the CCAA, the affected executives and former executives could argue that the deemed trust provisions under provincial legislation could apply to establish priority over other secured claims. By not acting and by not communicating the intention to continue to underfund to others who could act to initiate the wind up (i.e. the pension plan regulator FSCO), the Plan members were left in limbo. The Supreme Court of Canada, by not imputing a constructive trust in this situation, ostensibly allows this type of behaviour to persist post-Indalex.

The Indalex experience also shows that, even when the deficits in the plans were miniscule relative to the desired level of shareholder payments, management chose to actively work to avoid the payment obligation to maximize its payments to shareholders and related parties.

In the recent past, three federal private members bills sought to remedy the imbalance in the insolvency regime on pension issues (Bills 372,Bill C-384 and S-253)). All three Bills sought to

establish superpriority claims with respect to amounts that were required to be paid to a pension plan and any amount necessary to liquidate any unfunded liability or solvency deficiency. To accomplish this several provisions of the BIA and CCAA would have to be amended. For example, each Bill proposed additions to clause 60(1.5(a)) of the BIA and sections 81.5 and 81.6 dealing with receiverships. The key differences in approach between the two House of Commons drafts were (1) under Bill C-384 the plan must have been terminated; and (2) the amounts required to be paid upon termination of the fund must have been "required to be paid" under section 29 of the Pension Benefits Standards Act (or would have been required to be paid under the PBSA were the pension plan subject to the federal jurisdiction) whereas under Bill C-372 there was no statutory link to a methodology to guide the calculation of the unfunded liability or the solvency deficiency and the triggering of that liability was not contingent on the plan being terminated.

The benefit of a broad reference to unfunded liability and solvency deficiency is that it allows one to argue for coverage wherever the prescribed pension plan may be regulated. However, failing to define how the unfunded liability and solvency deficiency is determined in the insolvency legislation opens up the possibility for challenges from other creditors, the employer and possibly the trustee or monitor as to the proper methodology for the determination of the liability. There must be precision in defining the basis for determining the amount owed under the plan. But there also has to be flexibility built into the insolvency system to allow a judge to deem a plan wound up for the purpose of determining that liability. Simply ignoring funding obligations attaching to a pension plan should not enable management to escape responsibility to meet those obligations.

Referencing a particular regulator's minimum solvency funding standard can be problematic in that there is considerable variation across jurisdictions.

- The approach in Alberta and British Columbia preserves solvency funding requirements, but provides for solvency reserve accounts to allow withdrawal of actuarial excess or surplus if certain conditions are met. Despite preserving solvency funding, both jurisdictions have continued to provide forms of temporary solvency relief.

- Québec has eliminated the requirement for solvency funding for most ongoing plans altogether, but with the corollary introduction of a strengthened going concern model which includes a new stabilization provision related to the investment policy as well as accompanying changes to the rules governing portability and surplus rights.

- Ontario recently reduced the solvency funding target for DB plans to 85% of solvency liabilities. This was coupled with a new requirement to establish a funding reserve in the plan and a shortened amortization period for funding a going concern shortfall.

- Other jurisdictions (e.g., Manitoba, Nova Scotia) have released consultation papers seeking input on matters including solvency funding reforms. The possible reforms under discussion include changes similar to those introduced in Ontario.[8]

Rather than provide a direct reference to a particular jurisdiction's approach to solvency funding, the determination of the windup liability should be based upon the Canadian Institute of Actuaries Standards of Practice regarding windup valuations. The CIA regularly updates the assumptions to be used for actual and hypothetical windups and would therefore reflect as close to a market valuation as could be attained at the time of the insolvency proceeding and would not be dependent on a given jurisdiction's approach to the solvency funding issue.[9]

The financial services community will undoubtedly continue to argue that providing a superpriority to pension plan claims will cause havoc in credit markets. But, as noted above this has not been substantiated with hard data and the experience with insolvency proceedings between the Indalex Court of Appeal decision and the Supreme Court decision militates against this conclusion. They will also argue that it will create an unlevel playing field amongst creditors creating biases against creditors who have extended credit to companies on a basis that did not factor in pension plan liabilities as a secured priority.

An equally cogent argument is that employees deferred compensation on the promise of a pension benefit. They have committed extended periods of service contributing to the successes of their employers with the promise of the payment of a vested benefit in retirement. The pension regulatory system has served to bolster that belief by instituting immediate vesting and funding rules that plan sponsors were expected to adhere to. As shown in section 1(c) above, employers have chosen to bolster their corporate results by focusing on share buybacks when there was ample money available to meet pension funding obligations prior to making unnecessary shareholder payouts. The FSCO data also shows that the quantum of liability that is triggered through plan windups of insolvent plan sponsors is relatively small and arguably providing priority for such payments would have a negligible effect on the health of financial systems.

Moreover, there is precedent in Canadian law where corporate power is adjusted to reflect imbalances in bargaining power. The classic example is the labour relations system. To promote collective bargaining, labour relations legislation prohibits unfair labour practices on the part of the employer. Establishing a superpriority on pensions could be viewed as a means of balancing a system that is skewed in favour of corporate management and where, on a substantive basis, it can be demonstrated that executives have chosen short term awards in compensation triggered by shareholder payouts over meeting longer term corporate objectives and longer-term corporate obligations. One of the insolvency's regime answers to the information and power imbalance that has been inherent in the insolvency system could be the pension plan liability superpriority.

Not all creditors are created equal. It is a myth that the system treats everyone in a comparable manner. Senior management, external insolvency professionals and the courts regularly hear

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[8] Extracted from the Canadian Bar Association's submission to the Financial Sector Policy Branch, Finance Canada, dated July 13, 2018.

[9] For example, see the CIA's most recent educational note on windup assumptions at http://www.cia-ica.ca/docs/default-source/2018/218031e.pdf

from and involve creditors in the process that are viewed as having significant financial interests in the survival of a given company. Current insolvency legislation does not recognize that pensioners are likely the only stakeholders at the table with thirty or more years of commitment at risk, the only stakeholders that face a certain reduction in income for the rest of their lives, the only stakeholders at the table who have had no ability to negotiate the terms of their financial stake, and yet are not guaranteed full access to all relevant information and not guaranteed recognition as a unique group of stakeholders by the court. The VON Canada example above demonstrates the importance of pension stakeholders having an opportunity to provide input on decisions prior to as opposed to after the decisions have been made.

(b) Solvency Reserve Accounts (SRAs)

The introduction of solvency reserve accounts would be a positive step. CFP recognizes that there is a perceived asymmetry by employers given that they assume the risk of having to make solvency payments when a plan is in deficit and, in the low interest environment that has existed in the new millennium, these payments have been substantial. A significant increase in interest rates could result in solvency valuations revealing significant surpluses. What past history shows is that a draw down of surpluses in good times can lead to a funding crisis in bad times. Consequently, CFP supports a concept for surplus withdrawal from SRAs that parallels the amortization timeline used to defer solvency special payments. In other words, if an amortization is set at ten years, for example, to make special payments to meet a deficiency, then a draw down of surplus should be subject to the same constraint. A larger funding buffer can make pension contributions more predictable by reducing the need to increase pension contributions when there is an economic downturn or market correction.

The Department of Finance should also consider whether a cap on surplus in defined benefit plans makes any sense. As noted in the brief historical overview of the tax treatment of defined benefit plans, it was not until the 1980's that the concept of excess surplus was introduced and limits were placed on surplus accumulation. That was largely driven by the runaway inflation of the 1970's. Put in today's context, CFP questions the utility of a surplus cap in the ITA for broad-based defined benefit pension plans. If the Ministry of Finance's concern is on more customized defined benefit arrangements such as Individual Pension Plans, then the limit should be placed only on those types of arrangements and not on pension plans that are intended to cover the general workforce of an organization.

(c) Pension Funding Relief Criteria

Pension funding relief cannot be viewed in isolation. The data on executive compensation and shareholder payouts shows that money has been available in companies sponsoring underfunded defined benefit plans but senior management in many instances has decided to allocate funds to shareholders rather than meet their pension funding requirements. Again, using Indalex as an example, there are times when corporate behaviour should be reviewed prior to the granting of relief. In the Indalex example, not only was there a massive dividend payout but there was a sale

of strategic assets seemingly solely to meet a private equity manager's need to recover their investment and earn a premium over a three-year period.

Solvency relief should include a means test and the approval criteria should include an examination of cash and capital withdrawals from the company during the period under which the DB plan was underfunded. In certain circumstances during insolvency proceedings the court can look back five years to discern whether the actions of the company constituted preferential transactions and should be reversed. A similar look back authority should be placed in the hands of the pension regulator during the period a plan is underfunded. If there is evidence that there are unwarranted drains on capital made in lieu of meeting plan funding obligations, the pension regulator should have the authority to issue an order compelling payments to improve the funding level of the plan. Likewise, there may be instances where there are concerns as to the asset quality of plan holdings that may warrant regulatory intervention. The pension regulator should have the authority to issue orders respecting both funding and asset quality issues not dissimilar to authorities exercised by the Pension Benefit Guaranty Fund in the United States.

(d) Transfers to self-managed accounts

There have been several instances where distressed defined benefit plans have had difficulty purchasing annuities for retirees that replicate plan benefits. In certain jurisdictions, rigidity in the rules respecting asset transfers between plans effectively prevented plans from merging because the benefits in one plan differed from the benefits offered in another plan. These types of rigidities can serve to decrease the value of pension benefits when the objective of the pension regulatory system should be to maximize the opportunity to increase pension benefits within acceptable risk tolerances. Distressed pensions should be able to merge with qualified existing plans. CFP recognizes that this cannot be done to the detriment of the recipient plan and its beneficiaries. But opportunities to continue plans through merger aid in supporting the continued offering of pensions through employer-based pension plans.

Delays in allowing mergers can lead to substantial decreases in the value of pensions. The ideal remains having registered pension plans provide life-long pension benefits. However, the system must be sufficiently flexible to allow for alternatives, particularly when the market pricing of annuities is sub-optimal. In a plan windup situation, there should be the possibility to transfer assets into individual self-managed accounts in much the same way as occurs on a regular employment termination. There would be no taxation of the lump sum transfer. Only when there are payouts from the locked-in account would there be income tax levied. This is a common sense solution that should be pursued.

(e) Clarify benefit entitlement

The critical aspect with respect to conditionality of benefits is whether that conditionality is clearly communicated and understood. Further, there has to be a distinction between the base benefits that cannot be subject to differential treatment on plan termination and what may be termed supplementary or ancillary benefits. If a benefit such as indexation has been granted without qualification, it is a vested right and cannot be taken away. However, if indexation has been provided with the proviso that, if the plan terminates, that portion of benefits will no longer

be provided, why shouldn't that flexibility be available to the parties? By stating that all benefits must be provided regardless of the status of the plan, it may act as a disincentive to providing those supplementary benefits. Rigidity can lead to situations where such benefits are simply not extended because of the permanence of the promise. Context matters.

(f) Restrictions on corporate behavior

CFP supports restricting dividend payments, share redemptions and executive compensation packages where a company has a large pension deficit. However, this is a complicated question insofar as there are very large public corporations that operate privately registered subsidiary corporations in Canada. Classic examples of this can be found in the automotive sector where GM and Ford subsidiaries operate as private companies in Canada. There is not the same level of public disclosure for these subsidiary entities, yet the impact of a breach can be far reaching. CFP supports requiring any company, public or private, that has a large pension deficit to disclose to the pension regulatory authority and Corporations Canada (or the applicable provincial jurisdiction) its financial statements together with disclosure of any extraordinary transactions. The same criteria used to require disclosure of, for example, the top five executive's compensation in a public company could also be imposed on a private company with an unfunded registered pension plan. Year over year comparisons could be analyzed and if there is evidence that cash is being drained from the entity, the pension regulatory authority could be empowered to require additional payments to the pension fund. The distinction between private and public corporations could be preserved by not publishing private corporation information unless an enforcement action is required.

(g) Increased reporting and disclosure requirements

There is a growing awareness that increasing shareholder value cannot be the sole criterion governing corporate action. Corporations are given the rights and powers of an individual through legislation. But corporations cannot be sanctioned in the manner an individual can be sanctioned for wrongdoing. Shareholders are not the only stakeholders in a corporation. Over the past three decades, defined benefit plans' decline is not an isolated result. Wages have stagnated, group benefit provision for employees has declined and there has been large scale outsourcing and movement to part-time employment. As the drive for quarterly results dominates, there has been no hesitation on the part of many corporate entities to make short term decisions to the detriment of their respective enterprises.

The CBCA defines the scope of rights for a federally incorporated business. It shapes the scope of these businesses' responsibilities. One of the debates in the Indalex case was whether Indalex executives breached their fiduciary duty toward plan beneficiaries. The prevailing view espoused by those parties opposing the enforcement of the pension funding obligations was that, once in insolvency, in accordance with the two-hat doctrine, the executives had no fiduciary responsibility to continue to fulfill their obligation to plan members. The Court of Appeal rebuked the behaviour of the Indalex management team and its treatment of Plan beneficiaries confirming that the fiduciary responsibilities prevailed. The Supreme Court emphasized the failure to provide adequate notice and the conflict of interest between corporate duties and plan

administrator duties that the executives failed to resolve. At the least, they needed to appoint an independent plan administrator. They did nothing.

Corporate governance has to mean more than serving the interests of shareholders. A reporting requirement on policies that pertain to the interests of workers and pensioners would further clarify that workers and pensioners are more than a mere commodity contributing to the bottom line but rather are corporate resources to be valued and respected. The enhanced reporting aligns well with the Supreme Court decision in Indalex on the continuing fiduciary duty and would serve to spread the word to corporate and insolvency practitioners who are less likely to be aware of the nuances of pension administration and the ensuing responsibilities and more likely to be dismissive of plan members and pensioners roles and rights in the insolvency process and generally in day to day corporate functioning.

As mentioned in the preceding section, reporting requirements must be extended to include subsidiaries. Otherwise, the requirements can easily be skirted.

The above-noted fiduciary duty needs to be stated clearly and breaches must have consequences. In many cases, the pension fund and the related commitments represent one of the largest financial interests in a company. Yet, plan administrators and plan beneficiaries do not have access to company plans and cannot exert influence on company policies. If an outside investor carried the same financial weight through an investment in the company, he or she would likely have a seat on the board.

(h) Enhance look-back period

CFP supports including pension funding as a criterion to trigger a look back at dividend payments, share redemptions, executive bonuses and executive compensation increases. The concept as described in the Consultation Paper presents as a condition precedent that the pension plan had unfunded liabilities when it entered insolvency. One of the concerns is that the one year look back on dividend payments and share redemptions is too short a period. The look back should be defined by the period of time the plan was in deficit prior to insolvency. If we take yet again the Indalex example, the CCAA proceeding was in 2009. The dividend payout occurred June 1, 2007. Indalex made the decision to windup the salaried plan in 2006 while underfunded and simply refused to deal with the Executive Plan. A one year look back would not have captured the dividend payment nor would it have captured the alleged fraud in the preparation of the 2007 solvency opinion. Nor would it have captured the sell off of strategic assets in 2007. Reviewable transactions in the pension context should include any extraordinary transaction that had an impact on the operations and/or cash position of the business. There could very well be enforcement issues regarding clawbacks. Money distributed may not be available to be recaptured. That said, having the requirement in the BIA and CCAA could have an impact on corporate behaviour and prevent future indiscretions.

(i) Enhanced transparency in the CCAA process

One of the difficulties with the insolvency process in general is that the information the Court decides upon is provided by the applicant. The monitor or trustee does not attempt to validate the

information provided. The information is taken at face value. The monitor reports on the steps in the process and provides input to the court but the information upon which that is based is not independently verified. A duty of good faith imposed on all parties to the restructuring arguably already exists, but making it express provides another lever for a court to focus upon if evidence surfaces that calls into question the behaviour of one or more of the parties.

As noted previously in this submission, the inner circle is usually comprised of the applicant company, the monitor, major creditors including DIP lenders, possibly entities interested in purchasing all or a part of the applicant company and possibly a restructuring officer. A deal is worked on, a draft initial order is prepared and all is presented at a motion before a judge. Months of work goes into that motion. Outside the process, stakeholders such as pension members likely will not receive notice until just before the hearing and in the past often not at all. The initial order may suspend ongoing current and special contributions to the pension plan on top of it already being underfunded. And the deemed trust provisions in provincial legislation will be ignored unless raised by a representative of plan members or retirees. The Initial Order can be revisited during a call back period specified in the order, but that time is usually very short.

In the above scenario, it is virtually impossible for a representative of plan beneficiaries to obtain the information necessary to make an informed judgement on what is being proposed. Entrenching the right to participate in the process as early as possible increases the negotiating power of plan beneficiaries and will prevent the regular participants in the insolvency process from riding roughshod over plan beneficiaries' rights. Anecdotal feedback from practitioners who represent plan beneficiaries indicates that, in their opinion, early participation leads to a more balanced and equitable process. The VON Canada example described above shows that when plan members are represented, adverse action being contemplated against pension plan members may be avoided or minimized. The outcome of the Indalex case for the seven USW members of the Salaried Plan was that they received 100% of their accrued benefits while the remaining members of the Salaried Plan did not. Representation and access to information matters.

Because the insolvency process operates on a fast track, it is not always possible to obtain full disclosure as to why certain parties are participating in the process. There clearly is collusion in cases between creditors to orchestrate certain outcomes and it may not always be obvious to other stakeholders who is involved and why. There should be a requirement for full disclosure of the economic interest of creditors so that parties to the process can fully understand what interests are at play and to what end.

In short, an express duty of good faith, full creditor disclosure and limitations on the content of Initial Orders until pensioners and employee groups can fully engage would all be steps that would enhance the ability of pensioners and employee groups to advocate for their interests and negotiate with the parties on a more even footing. The duty of full disclosure should extend to related parties of the applicant. One of the exposures of the CCAA process is that related parties can be at the table without the knowledge of the other stakeholders and influence the process in favour of management without fully disclosing the extent and nature of the relationship.

3. CFP/NPF Proposals not contained in the Consultation Paper

(a) Backstop

CFP's position has always been that pensions are deferred wages, a commitment made over decades by employers, with only government legislation to protect them. Pensioners should receive their full pensions.

To that end, CFP proposes that a backstop be established. The backstop would take the form of a recurring annual refundable tax credit equal to the amount of pension lost by an individual due to insolvency. If measures implemented arising from this consultation result in pensions paid in full by the companies and the commercial interests around them, the tax credit would be zero. There would be no cost to the government and is CFP's preferred option. If, however, the government chooses not to place the full burden on companies for the commitment they have made to pensioners, the tax credit would be a means to partially assist the pensioner as he or she seeks to supplement pension income from other sources. It would be partial because its full effect depends on a number of factors including the marginal tax rate of that taxpayer and the resulting after-tax impact of the credit. It nevertheless would be a valuable backstop.

(b) Pension Insurance

CFP believes a robust pension insurance program that covers 100% of any pension loss could be a solution for federally regulated pensions; setting a best practice example for other jurisdictions. We accept and appreciate that the federal regulator is holding firm to 100% solvency targets for pension funding, but that is this time, this administration and this government. Even with a 100% solvency target, federally regulated plans are not all fully funded. The overwhelming trend is that jurisdictions are relaxing solvency requirements. In that reality, CFP supports solvency relief only if it is accompanied with a pension insurance scheme that covers 100% of any loss. CFP's analysis is that this is cost effective for companies and would afford full protection for pensioners.

4. Summary and conclusion

- The BIA and CCAA must be amended to lock in a superpriority for pension claims in the insolvency process.
- SRAs would be a positive step provided they are structured properly. Surplus withdrawal rights should be amortized over the same period as special payments.
- Removal of the excess surplus cap in the ITA is recommended. The cap’s introduction was triggered by rampant inflation and has no place in the current economic environment. Employers simply are not prone to overcontributing to defined benefit pension plans.

- CFP can support broad solvency relief if it is accompanied by a robust pension insurance program that ensures 100% of loss is covered.

- CFP can support special case solvency relief if properly structured. It should be means-tested and require adequate financial transaction disclosure. Pension regulator power should be enhanced to allow the compelling of payments in certain circumstances as well providing the authority to review asset quality and require changes in the asset mix to address quality concerns.

- CFP supports allowing lump sum direct transfers to retirees on plan termination on a tax deferred basis.

- CFP supports taking pro-active action to restrict share payouts, dividends, excessive executive bonuses, etc. when a pension plan is in a deficit position.

- CFP supports imposing increased reporting and disclosure requirements and emphasizes the need to expand coverage to subsidiaries and private corporations.

- The BIA and CCAA should permit look back periods that align with the period a pension plan is underfunded.

- CFP supports limiting the scope of Initial Orders until employees and plan beneficiaries are included in the process, requiring full creditor disclosure respecting their economic and related party interests with the applicant company and imposing an express duty of good faith on all participants in the insolvency process.