

# What About Federal Pension Claims?



## **The Status of *Pension Benefits Standards Act, 1985* and Pooled Registered Pension Plans Act Deemed Trust Claims in Insolvency<sup>1</sup>**

The priority of claims against insolvent employers for amounts owing under provincially-regulated pension plans and, in particular, plans governed by the *Pension Benefits Act* (Ontario) (the "**PBA**")<sup>2</sup>, has received a great deal of analysis over the past few years. These efforts reached an at least temporary peak upon the release of the decision of the Supreme Court of Canada (the "**S.C.C.**") in *Sun Indalex Finance, LLC v. United Steel Workers* ("**Indalex**")<sup>3</sup>, in February 2013. One issue left untouched by *Indalex* and the analysis surrounding it, however, is that of the priority of claims for amounts owing under pension plans governed by the federal *Pension Benefits Standard Act, 1985* (the "**PBSA**")<sup>4</sup> or the new federal *Pooled Registered Pension Plans Act* (the "**PRPPA**")<sup>5</sup>. Despite the deemed trusts created by the *PBSA* and the *PRPPA*, and despite some questionable case law concerning the effect of the *PBSA* deemed trust in particular, in this writer's view the answer is quite simple: in an insolvency proceeding, *PBSA* and *PRPPA* claims do not benefit from any super-priority trust or security apart from the protection explicitly created by the *Bankruptcy and Insolvency Act* (the "**BIA**")<sup>6</sup> and the *Companies' Creditors Arrangement Act* (the "**CCAA**")<sup>7</sup>.

### **Pension Protections under the *BIA* and *CCAA***

Priority charges in bankruptcy and receivership for a limited set of pension claims (under both *PBSA* plans and provincially-regulated plans) were created in July 2008 with the enactment of sections 81.5 and 81.6 of the *BIA*. Similar protection was added in September 2009 for *BIA* proposals and *CCAA* proceedings. Finally, with the coming into force of the *PRPPA* in December 14, 2012, protections for *PRPPA* amounts were added to the pension provisions in the *BIA* (for bankruptcy, receivership and proposals) and the pension provisions in the *CCAA*.

To take the example of receivership (and focusing on federal pensions), subsections 81.6 (1) and (2) of the *BIA* now read, in part, as follows:

#### **"Security for unpaid amounts re prescribed pensions plan – receivership**

81.6 (1) If a person who is subject to a receivership is an employer who participated or participates in a prescribed pension plan for the benefit of the person's employees, the following amounts that are unpaid immediately before the first day on

which there was a receiver in relation to the person are secured by security on all the person's assets:

a) an amount equal to the sum of all amounts that were deducted from the employees' remuneration for payment to the fund;

b) if the prescribed pension plan is regulated by an Act of Parliament,

i) an amount equal to the normal cost, within the meaning of subsection 2(1) of the *Pension Benefits Standards Regulations, 1985*, that was required to be paid by the employer to the fund, and

ii) an amount equal to the sum of all amounts that were required to be paid by the employer to the fund under a defined contribution provision, within the meaning of subsection 2(1) of the *Pension Benefits Standards Act, 1985*,

iii) an amount equal to the sum of all amounts that were required to be paid by the employer to the administrator of a pooled registered pension plan, as defined in subsection 2(1) of the *Pooled Registered Pension Plans Act*; and

. . .

## Rank of security

(2) A security under this section ranks above every other claim, right, charge or security against the person's assets, regardless of when that other claim, right, charge or security arose, except rights under sections 81.1 and 81.2 and securities under sections 81.3 and 81.4."

In terms of priority, pursuant to subsection 81.6(2), the pension claims charge ranks subordinate only to the *BIA* super-priorities in favour of unpaid suppliers, farmers (etc.) and employees. In the case of bankruptcies, *BIA* subsections 81.5 (1) and (2) have almost identical language to subsections 81.6 (1) and (2) with the exception that the charge in bankruptcy is also subordinate to statutory deemed trusts in favour of the Crown for source deductions (as preserved by subsection 67(3) of the *BIA*).

In terms of the scope of the charges, subparagraphs 81.5(1)(b)(i) and 81.6(1)(b)(i) refer us to subsection 2(1) of the *Pension Benefits Standards Regulations, 1985*<sup>8</sup>, which, in turn, defines "normal cost" as "the cost of benefits, **excluding special payments**, that are to accrue during a plan year, as determined on the basis of a going concern valuation" (emphasis added). Sections 81.5 and 81.6 of the *BIA* therefore only create super-priorities for any deducted but unremitted employee pension contributions, any unpaid employer defined-plan or pooled-registered-plan contributions and any unpaid normal costs. There is no super-priority under the *BIA* for unfunded pension liabilities (whether they be direct claims or special payments ordered by the Office of the Superintendent of Financial Institutions).

The pension protections in restructurings are found in *BIA* subsection 60(1.5) and *CCAA* subsection 6(6), which prohibit a court from sanctioning any proposal or plan that does not ensure payment of the same pension amounts as are protected by the *BIA* in bankruptcies and receiverships. Pursuant to *BIA* subsection 65.13(8) and *CCAA* subsection 36(7), a court also cannot approve a going-concern sale unless the same pension amounts will be paid out of the sale proceeds (or otherwise)<sup>9</sup>.

## **The Federal Pension Deemed Trusts**

The *PBSA* governs pension plans of employers that are federally regulated including, without limitation, those engaged in maritime shipping, aviation, broadcasting and banking, as well as plans of employers located in the Yukon, the Northwest Territories and Nunavut. Subsections 8(1) and (2) of the *PBSA* set up a deemed trust for amounts owing under a *PBSA* pension plan:

### **“Amounts to be held in trust**

8. (1) An employer shall ensure, with respect to its pension plan, that the following amounts are kept separate and apart from the employer’s own moneys, and the employer is deemed to hold the amounts referred to in paragraphs (a) to (c) in trust for members of the pension plan, former members, and any other persons entitled to pension benefits under the plan:

(a) the moneys in the pension fund,

(b) an amount equal to the aggregate of the following payments that have accrued to date:

i) the prescribed payments, and

ii) the payments that are required to be made under a workout agreement; and

(c) all of the following amounts that have not been remitted to the pension fund:

i) amounts deducted by the employer from members’ remuneration, and

ii) other amounts due to the pension fund from the employer, including any amounts that are required to be paid under subsection 9.14(2) or 29(6).

### **Where bankruptcy, etc., of employer**

(2) In the event of any liquidation, assignment or bankruptcy of an employer, an amount equal to the amount that by subsection (1) is deemed to be held in trust shall be deemed to be separate from and form no part of the estate in liquidation, assignment or bankruptcy, whether or not that amount has in fact been kept separate and apart from the employer’s own moneys or from the assets of the estate.”

Within the scope of this *PBSA* deemed trust are, among other amounts, any special payments prescribed to meet solvency requirements due on plan termination (pursuant to *PBSA* subsection 29(6)). The *PBSA* deemed trust is therefore more expansive than the protections provided in the *BIA* and the *CCAA*, which, as explained above, exclude special payments.

Pooled registered pension plans are defined-contribution pension plans, administered by financial institutions, for employees and self-employed persons who do not have access to workplace pension plans. The *PRPPA* governs pooled plans in federally-regulated industries and any such plans available to workers or the self-employed in the Yukon, the Northwest Territories and Nunavut. Section 31 of the *PRPPA* creates the

deemed trust:

### **“Amounts deemed to be held in trust**

31. (1) An employer must ensure that it keeps separate and apart from its own money all of the following amounts that have not been remitted to the administrator:

- (a) amounts deducted by the employer from employees' remuneration;
- (b) amounts of employer contributions; and
- (c) any other amounts required to be remitted to the administrator.

The employer is deemed to hold those amounts in trust for members of the plan.

### **If bankruptcy, etc., of employer**

(2) In the event of the winding-up, assignment or bankruptcy of an employer, an amount equal to the amount that by subsection (1) is deemed to be held in trust is deemed to be separate from and form no part of the estate in liquidation, assignment or bankruptcy, whether or not that amount has in fact been kept separate and apart from the employer's own moneys or from the assets of the estate.”

Unlike the *PBSA* deemed trust amounts, the amounts subject to the *PRPPA* deemed trust are limited to amounts already protected in the *BIA* and *CCAA*. This can largely be explained by the fact that pooled registered pension plans are, by definition, defined contribution rather than defined benefit plans. If, for example, we compare the *PRPPA* deemed trust to the protections in receivership given by the provisions of *BIA* section 81.6 excerpted above, we see that: the unremitted source deductions covered by *PRPPA* paragraph 31(1)(a) are already covered by *BIA* paragraph 81.6(1)(a); the employer contributions covered by *PRPPA* paragraph 31(1)(b) are covered by *BIA* paragraph 81.6(b)(ii); and the other amounts required to be remitted to the plan administrator, covered by *PRPPA* paragraph 31(1)(c), are covered by the new *BIA* paragraph 81.6(b)(iii).

The important points to note about the deemed trust language in both *PBSA* subsection 8(2) and *PRPPA* subsection 31(2) are: (i) that the deemed trusts only arise upon the occurrence of certain triggering events (bankruptcy, liquidation or winding-up); and (ii) that there is no explicit language giving the deemed trusts priority over other security interests.

### **Do the *PBSA* or *PRPPA* Create Protections in Addition to Those in the *BIA* and *CCAA*?**

As discussed above, the *PRPPA* deemed trust does not appear to extend to any amounts beyond those already protected under the *BIA* and *CCAA*, but the *PBSA* deemed trust is broader in its scope.

In answering the question of whether the *PBSA* deemed trust creates protections for pension claims beyond those found in the *BIA* and *CCAA*, we should note, first, that the fact that the *PBSA* deemed trust is a creature of statute is not fatal to it in insolvency. Since the *PBSA* deemed trust is not a trust in favour of the Crown, it is not reversed by *BIA* subsection 67(2). And, although there is a long line of case law stating that *BIA* paragraph 67(1)(a) does not exclude property subject to a provincial statutory deemed trust from the estate of a bankrupt, the reasoning of such cases would not apply to property subject to deemed trusts created by federal statute.

The deemed trust language in subsection 8(2) of the *PBSA*, unchanged since the enactment of the *PBSA* in 1986, is largely the same as the former deemed trust language in the *Income Tax Act* (the "*ITA*")<sup>10</sup> that the S.C.C., in *Royal Bank v. Sparrow Electric Corp.* ("*Sparrow Electric*")<sup>11</sup>, held did not create a priority over a general security interest properly perfected under provincial personal property security law. As stated by Justice Iacobucci for the majority in *Sparrow Electric*:

"98 It is open to my colleague to distinguish the fact situation in this appeal from the hypothetical priority contests I have mentioned on the ground that the Crown's interest in the inventory is unlike other charges against inventory in that it depends on the fictional device of deeming. What makes this case different, it might be said, is that the *ITA* deems to have been done what could have been done. On this understanding, it does not matter that the inventory was not actually sold and the proceeds were not actually remitted to the Receiver General, because ss. 227(4) and 227(5) of the *ITA* deem these things to have been done. But in my view, this answer cannot succeed because the inventory was not an unencumbered asset at the moment the taxes came due. It was subject to the respondent's security interest and therefore was legally the respondent's and not attachable by the deemed trust. As Gonthier J. himself says:

... [subsection 227(4)] does not permit Her Majesty to attach Her beneficial interest to property which, at the time of liquidation, assignment, receivership or bankruptcy, in law belongs to a party other than the tax debtor.

99 The deeming is thus not a mechanism for undoing an existing security interest, but rather a device for going back in time and seeking out an asset that was not, at the moment the income taxes came due, subject to any competing security interest. In short, the deemed trust provision cannot be effective unless it is first determined that there is some unencumbered asset out of which the trust may be deemed. The deeming follows the answering of the chattel security question; it does not determine the answer."

Amendments to the *ITA* (at subsections 227(4) and (4.1)) were made in 1998 in response to *Sparrow Electric*. These amendments had two main features: first, language was added to the effect that the deemed trust attached notwithstanding any other security interest (other than interests specifically prescribed by the regulations); and, second, the insolvency event trigger for the deemed trust was removed so that the deemed trust arose immediately upon the amounts becoming payable<sup>12</sup>. Similar changes were made at the same time to the deemed trust provisions in section 23 of the *Canada Pension Plan* (the "*CPP*")<sup>13</sup> and section 86 of the 1996 *Employment Insurance Act* (the "*EIA*")<sup>14</sup>, and would be made in 2000 to section 222 of the *Excise Tax Act* (the "*ETA*")<sup>15</sup>.

In contrast, although there were extensive amendments made to section 8 of the *PBSA* in 1998 and 2010 (as well as amendments made by the *PRPPA* in 2012), none of these touched subsection 8(2). No explicit priority language was ever added and the insolvency event trigger remains to this day. Parliament therefore seems intent not to create any super-priority in the *PBSA* apart from what it created for *PBSA* plans in the 2008 and 2009 amendments to the *BIA* and *CCAA*.

The S.C.C.'s *Sparrow Electric* decision was released on February 27, 1997. Shortly prior, on January 9 of that same year, the Ontario Court of Justice, General Division (Commercial List) released a decision in *Neal v. Toronto Dominion Bank* ("*Neal*")<sup>16</sup> which held that a general security interest ranked subordinate to a deemed trust claim under the *PBSA*. The court in *Neal* followed the S.C.C.'s 1980 decision in *Dauphin Plains Credit Union Ltd. v. Xyloid Industries Ltd.* ("*Dauphin Plains*")<sup>17</sup> which

held that a general security interest was a floating charge, which only became crystallized upon enforcement, and which, therefore, did not rank ahead of deemed trust claims under the *CPP* or the *Unemployment Insurance Act, 1971*. What was not raised in *Neal*, but had, by that time, already been addressed by the Alberta Court of Appeal in its *Sparrow Electric* decision, was the fact that *Dauphin Plains* was decided prior to the enactment of a *Personal Property Security Act* in the relevant jurisdiction (Manitoba). In its *Sparrow Electric* decision, the Alberta Court of Appeal held that a security interest properly perfected under the Manitoba *Personal Property Security Act* was a fixed and specific charge. The S.C.C. in *Dauphin Plains* had held that deemed trust claims for pension plan and unemployment insurance deductions did not rank ahead of a fixed and specific charge like it did a floating charge:

"25 . . . the claim for pension plan and unemployment insurance deductions cannot affect the proceeds of realization of property subject to a fixed and specific charge. From the moment such charge was created, the assets subject thereto, were no longer the property of the debtor except subject to that charge. The claim for the deductions arose subsequently and thus cannot affect this charge in the absence of a statute specifically so providing. However, the floating charge did not crystallize prior to the issue of the writ and the appointment of the receiver. In the present case it makes no difference which of the two dates is selected, both are subsequent to the deductions."

Following this reasoning in *Dauphin Plains*, the Alberta Court of Appeal held that deemed trust claims under the *ITA* did not rank ahead of a general security interest perfected under provincial personal property security law because such a security interest was a fixed and specific charge.

It therefore appears that the pension claims priority aspect of *Neal* was bad law when it was made, since the decision did not take into account the effect of the *Personal Property Security Act* (Ontario) (the "*PPSA*")<sup>18</sup> nor consider, let alone follow, the Alberta Court of Appeal's *Sparrow Electric* decision. In any event, the S.C.C.'s subsequent decision in *Sparrow Electric* (upholding the Alberta Court of Appeal's ruling) shows conclusively that the pension priority reasoning in *Neal* is fatally flawed.

The above application of the *Sparrow Electric* reasoning to the *PBSA* deemed trust yields the same results as application of common rules of statutory interpretation. Given that the pension provisions of the *BIA* and *CCAA* came into force much later than section 8 of the *PBSA*, normal interpretation would require that the later legislation be deemed to be remedial in nature. Likewise since these provisions of the *BIA* and *CCAA* are the more specific provisions, normal interpretation would take them to have precedence over the general. Finally, the limited scope of the protection given to pension claims in the *BIA* and the *CCAA* would, by application of the doctrine of implied exclusion, suggest that Parliament did not intend there to be any additional protection<sup>19</sup>. In enacting *BIA* subsections 60(1.5) and 65.13(8) and sections 81.5 and 81.6 and *CCAA* subsections 6(6) and 36(7), while not amending subsection 8(2) of the *PBSA* (by adding explicit priority language or by removing the insolvency trigger), Parliament demonstrated the intent that pension claims would have protection in insolvencies and restructurings only to the limited extent set out in the *BIA* and *CCAA*.

There are three additional hurdles for anyone who wishes to assert a *PBSA* deemed trust claim against an insolvent company for amounts not otherwise protected under the *BIA* or *CCAA*. First, in the case of a bankrupt company, *BIA* section 136 contains

no spot on the priority scheme for pension claims. Second, by the operation of *BIA* subsection 66(1), the section 136 priority scheme also applies to Division I proposals<sup>20</sup>. Third, as commented on, in *obiter*, by Justice Farley in *United Air Lines Inc.*<sup>21</sup>, the insolvency trigger in subsection 8(2) of the *PBSA* refers only to “liquidation, assignment or bankruptcy,” but not to restructuring. Thus, even, if the *PBSA* deemed trust was sufficient to otherwise prime secured creditors, there is doubt whether the deemed trust would even arise in a *BIA* proposal or *CCAA* plan.

## Conclusion

Although the *PBSA* deemed trust covers classes of pension claims not protected in the *BIA* or *CCAA*, the archaic language of this deemed trust does not create an interest that can prime a properly perfected contractual security interest. The *PBSA* deemed trust therefore does not provide additional protection or priority for pension claims against an insolvent employer (beyond the protections provided in the *BIA* and *CCAA*). There is thus no parallel between the protection provided by the *PBSA* deemed trust and any protection that *might* be provided by the *PBA* deemed trust (in conjunction with subsection 30(7) of the *PPSA*), as dealt with in *Indalex*<sup>22</sup>. These limits to the *PBSA* protection do not appear to be an oversight by Parliament as the *PBSA* is one of the very few federal deemed trust statutes that was not amended in response to *Sparrow Electric*.

Even though the *PRPPA* subsection 8(2) deemed trust language largely tracks the analogous language in the *PBSA*, the amounts actually covered by the *PRPPA* deemed trust do not appear to extend beyond the amounts already protected in the *BIA* and the *CCAA*, and thus the effect of the *PRPPA* deemed trust in insolvency in relation to secured claims is likely a moot point. That being said, a number of provinces are expected to introduce their own pooled registered pension plan regimes, and, as a result of these and the *PRPPA* regime, a great number of Canadian workers will likely have access to pensions where they never did before. The corollary is that a great number of Canadian employers will become indebted to pension plans where they never were before (especially small and medium enterprises, relatively more prone to insolvency). We can therefore expect the number of super-priority pension claims in insolvencies and restructurings to rise in the future.

## Footnotes

1 An expanded version of this article appeared in *National Creditor Debtor Review*, September 2013, Volume 28, Number 3.

2 R.S.O. 1990, c. P.8

3 *Sun Indalex Finance, LLC v. United Steelworkers*, [2013] S.C.J. No. 6 (S.C.C.); reversing *Indalex Ltd. (Re)*, [2011] O.J. No. 1621 (Ont. C.A.); reversing *Indalex Ltd. (Re)*, [2010] O.J. No. 974 (Ont. S.C.J.—Commercial List); and reversing in part *Indalex Ltd. (Re)*, [2011] O.J. No. 3959 (Ont. C.A.). For a discussion of *Indalex*, see the writer’s earlier article “After Indalex: Pension Claims under the New *CCAA*,” published in *Collateral Matters*, May 2013 (and in *National Creditor Debtor Review*, June 2013, Volume 28, Number 2).

4 R.S.C. 1985, c 32 (2nd Supp)

5 S.C. 2012, c. 16

6 R.S.C. 1985, c. B-3

7 R.S.C. 1985, c. C-36

9 Strictly speaking, *CCAA* subsection 36(7), as presently drafted, does not give this protection to pension amounts due to the fact that it cross-references the wrong paragraphs of section 6. The writer has, however, argued elsewhere that this is only due to an acknowledged drafting error and the subsection ought to be interpreted and/or corrected to give the pension protection as Parliament intended (see “After Indalex: Pension Claims under the New *CCAA*”, note 3 *supra*, at pages 2 to 3).

10 R.S.C. 1985, c. 1 (5th Supp). The former Subsections 227(4) and (5) read as follows:

“(4) Every person who deducts or withholds any amount under this Act shall be deemed to hold the amount in so deducted or withheld in trust for Her Majesty.

(5) Notwithstanding any provision of the *Bankruptcy and Insolvency Act*, in the event of any liquidation, assignment, receivership or bankruptcy of or by a person, an amount equal to any amount:

(a) deemed by subsection (4) to be held in trust for Her Majesty, or (b) deducted or withheld under an Act of a province with which the Minister of Finance has entered into an agreement for the collection of taxes payable to the province under that Act that is deemed under that Act to be held in trust for Her Majesty in right of the province shall be deemed to be separate and apart from and form no part of the estate in liquidation, assignment, receivership or bankruptcy, whether or not that amount has in fact been kept separate and apart from the person's own moneys or from the assets of the estate.”

11 *Royal Bank v. Sparrow Electric Corp. (sub nom. R. v. Royal Bank)*, [1997] 1 S.C.R. 411 (S.C.C.); affirming *Royal Bank v. Sparrow Electric Corp.*, [1995] 2 C.T.C. 445 #2, 33 C.B.R. (3d) 34 (Alta C.A.); reversing *Royal Bank v. Sparrow Electric Corp.*, [1994] 9 W.W.R. 338 (Alta Q.B.) and *Royal Bank v. Sparrow Electric Corp.*, (1993) 19 Alta. L.R. (3d) 183, [1995] 1 C.T.C. 101 (Alta. Q.B.).

12 These amendments were made, effective as of June 15, 1994, by the *Income Tax Amendments Act, 1997*, R.S.C. 1998 c.19. The history and intent of these changes as responses to *Sparrow Electric* was summarized by the S.C.C. in *First Vancouver Finance v. Minister of National Revenue*, (2002) 2002 SCC 49, [2002] S.C.R. 720 (S.C.C.) at paragraphs 25 to 29.

13 R.S.C. 1985, c. C-8. As with the 1998 amendments to the *ITA*, these amendments to the *CPP* were made by the *Income Tax Amendments Act, 1997* (see note 12 *supra*).

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14 S.C. 1996, c. 23. Like the contemporaneous amendments to the *ITA* and the *CPP*, the changes to the deemed trust language in the *EIA* were made by the *Income Tax Amendments Act, 1997* (see note 12 *supra*).

15 R.S.C. 1985, c. E-15. In June, 1999, the Minister of Finance released explanatory notes to, among other pending statutes, the *Sales Tax and Excise Tax Amendment Act, 1999*, R.S.C. 2000 c. 30, which introduced the changes to, among other provisions, *ETA* Section 222. These notes state that the amendments are a response to *Sparrow Electric* as were similar amendments made previously to Section 227 of the *ITA*, and, specifically, that the changes clarify that the Crown has priority through its trust over any other security interest and that amounts subject to the trust are deemed to be held separately and apart at all times (and not just after a triggering event of liquidation, assignment, receivership or bankruptcy). See [http://www.fin.gc.ca/drleg/99-104\\_2e.pdf](http://www.fin.gc.ca/drleg/99-104_2e.pdf) at page 101.

16 *Neal v. Toronto Dominion Bank*, (1997) 1997 CarswellOnt 403, 25 O.T.C. 142 (Ont. C.J. Gen. Div. [Commercial List]).

17 *Dauphin Plains Credit Union Ltd. v. Xyloid Industries Ltd.*, [1980] 1 S.C.R. 1182 (S.C.C.)

18 R.S.O. 1990, c. P.10

19 This writer has argued elsewhere that the doctrine implied exclusion has been consistently applied by the S.C.C. to matters of *CCAA* priorities. See

“After Indalex: Pension Claims under the New *CCAA*”, note 3 *supra*, at pages 7 to 8.

20 The *BIA* section 136 priority scheme may or may not also apply in the case of a going-concern sale in a proposal proceeding because subsection 66(1) was not amended to include the new concept of going-concern sale introduced by the 2009 amendments.

21 *United Air Lines Inc., Re*, (2005) 9 C.B.R. (5th) 159 (Ont. S.C.J. [Commercial List]) at para 11.

22 Emphasis on the word “might” is added because it is not clear that the *PBA* deemed trust does provide priority beyond the protections provided in the *BIA* and *CCAA*. As the writer has argued elsewhere, *Indalex* was decided without application of the September, 2009 amendments to the *CCAA* and tells us nothing about the effect of those amendments. In light of those amendments, the writer has argued, the *PBA* deemed trust ought no longer be considered to provide priority in a *CCAA* proceeding. See “After Indalex: Pension Claims under the New *CCAA*”, note 3 *supra*.