

PENSIONS & BENEFITS

Pension plan sponsors can pay plan expenses from fund: *Kerry*

Although the rights of plan sponsors have been expanded, employers should still carefully analyze their plans to ensure the language doesn't restrict reimbursement

By Mitch Frazer

A recent long-awaited decision of the Ontario Court of Appeal clarifies important legal issues for pension plan sponsors who are considering paying plan expenses out of the fund, changing their plan structure or communicating to plan members.

The *Kerry* decision

In *Kerry (Canada) Inc. v. DCA Employees Pension Committee*, [2007] O.J. No. 2176, a defined benefit (DB) plan was established in 1954 and the assets of the plan were held in a trust.

From the plan's inception through to the end of 1984, the company paid all plan expenses. Beginning in 1985, the company began paying third-party expenses from the fund and taking contribution holidays.

In 2000, the plan was amended to add a defined contribution (DC) component. New employees were required to participate in the DC component, and existing employees were given a one-time option to convert the value of their DB pension.

After the 2000 amendments were introduced, a committee of former employees asked the Superintendent of Financial Services (Superintendent) to investigate alleged irregularities in the administration of the plan. The Superintendent issued a Notice of Proposal to make an order requiring the company to reimburse the fund for expenses paid from the fund that were not incurred for the exclusive benefit of plan members.

Through a series of appeals, the

Financial Services Tribunal (see "Can plan expenses be paid from the fund?" in the March 24, 2006, issue of *The Lawyers Weekly*) and then the Ontario Divisional Court (see "Decision makes paying plan expenses out of pension funds more difficult" in the May 19, 2006, issue of *The Lawyers Weekly*) considered the following issues:

(i) the ability to pay plan expenses from the fund;

(ii) the use of surplus assets in the DB component of a plan to pay current service costs in respect of the DC component of the plan (cross-subsidization); and

(iii) what constitutes proper notice of an adverse amendment. The matter was then appealed to the Ontario Court of Appeal.

Plan expenses

The Court of Appeal held that the company was permitted to pay most of the plan expenses from the fund. Since neither the Ontario *Pension Benefits Act* (PBA) nor legal principles require a company to pay plan expenses, the court held that the terms of the plan documentation (the plan text and the trust agreement taken together) must govern.

The court also held that if a plan text is silent in respect of payment of plan expenses, this does not create a legal obligation for a company to pay expenses, and a past practice of voluntary payment of expenses does not create a legal obligation to continue this practice.

However, the court did decide that payment for advice regarding the addition of a DC option was for the company's own benefit and that it was obliged to pay for this advice.

Contribution holidays and cross-subsidization

The court held that surplus in the DB component of a pension plan could be used to satisfy a company's contribution obligation regarding the DC component of that plan. The fact that plan membership was expanded through inclusion of a new category of member did not alter the company's right to take contribution

holidays as long as the members in the DC component were beneficiaries of the entire fund.

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Finally, the court specifically contradicted the Ontario Divisional Court and held that the introduction of a DC component to the plan does not create a second plan.

Notice of plan amendment

The court held that the company had an obligation to give notice of the plan amendment that created the conversion option and that a conversion from DB to DC was an adverse amendment because of the uncertainty and risk of such a change.

The court also held that although the company did not give plan members adequate notice of the conversion option, failure to do so did not result in an amendment being non-registrable or void since the PBA gives the Superintendent

the discretion to register an amendment even when inadequate notice has been given.

Implications of *Kerry*

Kerry clarifies a plan sponsor's right to pay plan expenses from a pension fund, the use of DB surplus

to fund employer contributions under the DC component of the plan and the notice requirements on a plan conversion.

While the right of plan sponsors to pay plan expenses from the

fund has been expanded, employers will still have to carefully analyze their historical plan and trust documentation to ensure that the language does not restrict reimbursement.

Plan sponsors will also have to carefully consider what types of fees they can legally charge to the pension fund. Employers will be required to pay expenses that are clearly for their benefit.

Cross-subsidization turns on plan documentation and may be permitted if members are beneficiaries under both components of the same plan and if the plan language permits contribution holidays and cross-subsidization. Therefore, cross-subsidization will be permitted if a DC conversion is properly structured.

Plan sponsors should ensure that communications are consistent with pension legislation and plan documents, and that they properly describe the effect of any changes or members rights concerning the plan.

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