

Pensions and Insolvency Law: A Functional Comparison of Canadian, U.S. and U.K. Legal Regimes

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Regulation of Insolvency Risk

- Assets separated from employer's
- Regular contributions required
- Professional determination of contribution levels
- Duties of good faith and care
- Ontario guarantees benefits \$1000/month - PBGF



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Residual Insolvency Risks - Pension Plans

- Contribution Delinquency
- Funding Deficiency



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Canada

- Pre-reform - liquidation
 - Employee wages
 - 4th ranking preference
 - Pension contributions
 - Not included in preference
 - Unsecured claims
- Restructuring
 - Er req'd to pay wage arrears
 - Pension contributions excluded



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Reform Rationales

- Employee as contracting party
 - No protection against bankruptcy
 - No risk premium
 - Secured creditor allocates risk to ees
 - Even if bargain premium
 - *Ex post* increase in risk
 - Inefficient bargain
 - Others = superior knowledge & bargaining power
 - No diversification of risk



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Consequences

- Rationales accepted
 - Doesn't dictate reform of insolvency
 - Other jurisdictions have different regimes – protection in pension law
 - Why Canada chose insolvency law as site of reform?



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Canada

- Post-reform - liquidation
 - Contributions (narrow def'n)
 - Secured claims
 - Rank behind wage claim, unremitted source deductions
 - Includes
 - Er normal cost + ee contributions deducted from salary
 - Excludes
 - Special payments or deficiency on plan termination
 - Bankruptcy trustees/receivers liable



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Canada

- Post reform – restructuring
 - Payment of contributions required
 - Excludes special payments
 - Subject to compromise
 - Regulator must approve
- Part of larger reform re wages
 - Tax funded Wage Earner Protection
 - \$3,000 cap
 - Super priority for unpaid wages
 - \$2,000 cap



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U.S.

- Private Sector Benefits Insured
 - PBGC - \$47,659/year
- Pre-petition contribution arrears
 - Fourth ranking preference claim
 - Subordinate to any secured claims
- Solvency deficiency claims by PBGC – secured or unsecured?



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U.K.

- Benefits insured – PPF
- Contribution arrears
 - Second rank claim
 - behind fixed asset secured creditors
 - Gov't insurance avail to fund contribution arrears
- Balance of claims unsecured
 - PPF claim



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Contrast

- Canada
 - Insurance 1 province
 - \$12,000/yr
 - Contributions
 - 4th rank secured
 - All assets
 - Solvency claim
 - Unsecured
- U.S.
 - Nationwide insurance
 - \$47,000+ /yr
 - Contributions
 - Unsecured
 - 4th rank preference
 - Insurer's solvency claim
 - Unsecured



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Contrast

- Canada
 - Insurance single province
 - \$12,000/yr
 - Contributions
 - 4th rank secured
 - All assets
 - Solvency claim
 - Unsecured
- U.K.
 - Nationwide Insurance
 - Some caps
 - Contributions
 - 2nd rank claim
 - Govt. insurance
 - Insurer's solvency claim
 - Unsecured



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Why Differences?

- Canada's constitution
 - Split legislative authority
 - Fed – insolvency
 - Prov. – ee/er relations & pensions
 - Insurance expensive difficult to design
 - Fed lacks authority to control funding
 - Reluctance to assume resp. where regulation other hands
- U.K. – unitary legislative authority
- U.S. – federal authority over both



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Arrears – Deficiency Different Approaches

- Why insurance?
 - Responsible for regulation of funding
 - Solvency deficiencies dwarf assets of distressed employer
 - Change in priority - no beneficial effect for plan members
 - Secured creditors restrict lending
 - Cost-benefit not favourable



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Effects of Change – Improvement?

- Substantial legislative change
- Actual change – asset dependent
 - increase in contribution collection?
 - Credit restricted?
 - Solvency deficiency issue remains
- Restructuring changes positive
 - Flexibility over repayment terms avoids plan termination



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Possible effects

- Increase in secured creditor monitoring
 - Daniels and Triantis (1995)
- Requiring contribution funding mechanisms to protect security
 - Concern about preference
- Pay or play in restructuring
- Empirical study needed



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