



Legal Issues in Managing Your Benefits Plan

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Introduction

- Administrators of benefit plans, such as employers and boards of trustees (both joint and single sponsor) should be aware of the potential pitfalls in administration.
- This presentation reviews some of the recent case law and legislative changes affecting benefit plans.



Presentation Overview

- Lessons for Day-to-Day Administration
 - Liability for Failure to Enrol
 - Beneficiary Designations
 - Entitlement Issues
- Lessons from Nortel
- New ELHT Rules
- Update on Retiree Benefit Litigation



Enrolment Issues: Case Study #1

- At the time of hire an employee is provided with a brochure about the group life insurance plan sponsored by the employer and told he should enrol when he becomes eligible.
- The employee becomes eligible but does not enrol within the "enrolment period" - outside of the enrolment period, enrolment requires satisfactory medical evidence. The employee dies unexpectedly.
- The day before his death he had finally decided to apply for insurance but failed to submit proof of eligibility.



Does the employer have any liability?



Enrolment Issues: Case Study #1

Grams Estate v Maple Leaf Metal Industries Limited

- The employee's estate sought payment under the policy. The insurer denied the claim.
- The estate then sought compensation from the employer on the basis that it was negligent in administering the group insurance plan.
- The Court held that the employer was negligent because it did not provide sufficient information about the insurance coverage to the employee.
- The employee was also negligent due to his failure to make appropriate enquiries.



Enrolment Issues: Case Study #1


TIPS:

- Employers should consider, as part of the orientation process, providing a memo to each new employee **highlighting the timelines for enrolling in group benefit plans, and the consequences of failing to meet those deadlines.**
- Employers should also consider obtaining written acknowledgments from new employees that they have received information regarding applicable benefit plans; and, where participation has been declined by an employee, written confirmation of that decision.



Enrolment Issues: Case Study #2

- For purposes of eligibility to participate in benefit plans, “eligible employee” is defined as full-time employee or permanent part-time employee.
- If coverage waived, an employee could join at later date subject to “penalties” and restrictions.
- Employee originally hired on part-time basis and waived benefit coverage.
- Employee subsequently becomes permanent full-time employee.



Does the employee get a second opportunity to enrol in benefit plans without penalties and restrictions because of change in status?



Enrolment Issues: Case Study #2

Toronto District School Board v C.U.P.E. 4400

- Change in employment status gave the employee a fresh entitlement to enrol in the benefit plans, without penalties and restrictions.



Enrolment Issues: Case Study #2

TIPS:

- Do any “fresh entitlement” issues arise in your workplace?
- If so, implement processes to ensure key information is conveyed to employees when a “fresh entitlement” situation occurs.



Beneficiary Designations: Case Study #1

- Former wife was married to employee for 13 years.
- Former wife was the designated beneficiary under the employee’s group life insurance policy and pension plan.
- When the parties separated they entered into a separation agreement containing broad releases respecting all property claims they might otherwise be able to make against each other.
- Beneficiary designation under the life insurance was never changed.
- Employee died.



Does the separation agreement override the life insurance beneficiary designation?



Beneficiary Designations: Case Study #1

Conway v Conway Estate, 2006

- The Court concluded the separation agreement did not amount to a “declaration” to alter or revoke a beneficiary designation as required under the *Insurance Act*.
- Specific reference to the plan was necessary to make the revocation effective.
- The Court also refused to impose a constructive trust or consider the allegation that Brian Conway intended to change his beneficiary designation for the purposes of the life insurance benefit.
- The Court also considered the *Succession Law Reform Act* and found the release in the separation agreement was insufficient to revoke Deborah Conway as the designated beneficiary of the pension death benefits.



Beneficiary Designations: Case Study #1

TIPS:

- General communications should encourage employees to review beneficiary designation in conjunction with “life events”.
- All beneficiary designations must comply with applicable laws in order to be effective. Thus, plan administrators must understand the governing legal “regime”.
- Plan administrators must do their homework before paying out benefits to beneficiaries. Relevant documentation must be reviewed before making any payments or proclaiming entitlement, particularly in marriage breakdowns.



Beneficiary Designations: Case Study #2

- Husband and Wife #1 completed a separation agreement. Husband was required to designate Wife #1 as beneficiary of husband’s life insurance policy for 1 year.
- Husband then married Wife #2.
- Husband prepared a new will, leaving his estate to Wife #2. he also appointed Wife #2 as power of attorney.
- Husband became ill, Wife #2 exercised power of attorney for a number of years.
- Wife #2 continued to pay the life insurance premiums (including payment from her own funds) believing she was the beneficiary.
- Husband never changed beneficiary designation under policy.
- Husband died.



Is Wife #2 entitled to the proceeds from the insurance policy?



Beneficiary Designations: Case Study #2

Richardson Estate v Mew, 2009 Ontario Court of Appeal

- Wife #2 claimed she would have used power of attorney to stop paying premiums or changed the beneficiary designation if she knew she was not the beneficiary. As such, payment of proceeds to Wife #1 (Mew) would be unjust enrichment.
- Court concluded that there was no unjust enrichment - there was a legal basis ("juristic reason") for Mew's enrichment - the designation.
- Power of attorney is a fiduciary position. Wife #2 could not have used power of attorney to change beneficiary designation - as not acting in best interests of husband by doing so.
- Again, the mutual release in the separation agreement was not enough to change Wife #1's designation as beneficiary.



Beneficiary Designations: Case Study #2

TIPS:

- Extra caution must be taken when instructions are received under a power of attorney.
- If an employer or plan administrator receives a request through a power of attorney to change a beneficiary designation:
 - if the donor remains capable, seek confirmation that the attorney acts under instruction,
 - if the donor is (or may be) incapable, advise attorney to seek Court approval.



Entitlement Issues: Case Study

- Employee advised employer of his "retirement" at age 54.
- Employee was not entitled to commence pension benefits at time of retirement. He elected a deferred pension.
- Employer offered certain health benefits to retirees.
- Employer denied benefit coverage to the former employee because he had not "retired".



Is the former employee entitled to retiree benefits?



Entitlement Issues: Case Study

Berthiaume v City of Windsor, 2009

- By-laws relating to health care benefits had historically defined "retired employee".
- Historical by-laws were repealed. No replacement by-law or other documentation limited eligibility to retiree health care benefits to former employees who immediately commenced receipt of pension benefits.
- Court declared that the former employee was entitled to retiree health care benefits.



Eligibility Requirements: Case Study

TIPS:

- Ensure that eligibility restrictions are set out in constituting documentation (policies, by-laws, etc.) AND communicated to employees.
- Applies to all types of eligibility requirements. E.g., definition of spouse and definition of child.



Lessons from Nortel

- In January 2009, Nortel Networks entered court proceedings under the *Companies' Creditors Arrangement Act*, leaving the status of employee pension and benefit plans uncertain.
- **Benefits issues:**
 - Continuation of benefits payments
 - Self-insured disability program
 - Health and Welfare Trust

Lessons from Nortel

- On March 31, 2010, the Court approved a Settlement Agreement which insures that the following benefits will be paid in full until the end of 2010:
 - Health
 - Dental
 - Life Insurance
 - Survivor Income Benefits
- What happens after December 31, 2010?
 - HWT allocation
 - Future benefit plans

Employee Life and Health Trusts (ELHTs)

BACKGROUND

- US experience: VEBAs
- CAW negotiations with GM and Chrysler
- Current: Health and Welfare Trust (IT85R2)
- February 26, 2010: Federal Minister of Finance announced a proposal to amend the *Income Tax Act* to allow the creation of a new means of delivery of health and welfare benefits: the ELHT.
- August 27, 2010: release of revised version of legislation



Employee Life and Health Trusts (ELHTs)

The creation of ELHTs under the ITA addresses, among other things, two obstacles that existed under the current HWT regime:

- Pre-funding of benefits through large lump-sum contributions and other debt instruments
- Deductibility of those contributions by employers



Employee Life and Health Trusts (ELHTs)

FEATURES:

- Can be used for:
 - both actives and retirees, and their dependents
 - any combination of group sickness or accident benefits, private health services plan benefits or life insurance benefits
- ELHTs are taxable
 - but all expenses, including benefit costs, are deductible from trust income
- No change to the taxability of benefits
 - Life insurance benefits remain the only benefit taxable in hands of employees

ELHTs: Features (cont'd)

- Contributions by employer are deductible provided they meet the criteria
 - Lump sums are deductible over a period of years
 - "...to the extent that the amount may reasonably be regarded as having been contributed to fund designated employee benefits payable in the year..."
- MEPPs are treated differently

ELHTs: Features (cont'd)

Other

- Benefits must be supported by a plan of insurance, which includes a self-funded arrangement.
- The sole purpose of the Trust must be to provide Designated Employee Benefits.
- It must be a Canadian resident trust.
- The trust must be maintained primarily for the benefit of ordinary employees not just "key employees" which will be a defined term under the proposed rules. Key employees must be treated the same as all other employees.



ELHTs: Features (cont'd)

Other (cont'd)

- To qualify, the trust agreement must provide that the employer has no right to distribution of surplus from the trust.
- Employer representatives may not constitute a majority of the trustees of the trust.
- If passed, the proposal will apply to trusts established after 2009.



ELHTs: Features (cont'd)

- Multi-employer plans – special contribution deductibility rules permit deduction if:
 - At least 15 employers participate or at least 10% of the employee beneficiaries are employed by more than 1 PE
 - Collective agreement
 - Contributions are made by reference to hours worked by individual or some other individual-specific metric



ELHTs: Features (cont'd)

- Expect to see ELHTs proposed by employers who are motivated to remove retiree health care liabilities from their balance sheets
- Issues:
 - Security of pre-funding;
 - Sufficiency of pre-funding
- Existing HWTs?



Update on Retiree Benefit Litigation

- Leading case remains Supreme Court decision in *Re Dayco*, 1993.
- Court found that right to promised benefits vested or crystallized at retirement.
- Employers must expressly reserve right to make changes to level of benefits.
- The contract in effect at retirement governs post retirement relationship.



Bennett v British Columbia, 2009

- Class action involving 27,000 retirees.
- Employer unilaterally made reductions to the retiree benefits plan.
- Class claimed that the changes constituted a breach of fiduciary duty and a breach of the employment contract.



Bennett v British Columbia, 2009 (cont'd)

- The Court found that benefits did not vest in retirees.
- Retirement letters, application forms, information seminars, etc., did not create contractual obligations regarding retiree benefits.
- No breach of fiduciary duty, despite vulnerability.
- No reasonable expectation that employer would act in retirees' best interests at the expense of public interest.



Nadolny v Peel, 2009

Acreman v Memorial University, 2010

- Two class actions commenced in different provinces.
- Both alleging unilateral increase in benefit plan premium cost sharing breached fiduciary duties and was a negligent misrepresentation.
- Claims relied on prior communication to effect that premiums would not increase.



Nadolny v Peel, 2009

Acreman v Memorial University, 2010

- **Nadolny**: Court did not certify class action – finding no common issues.
Duties owed to retirees would be determined in light of various communications over many years.
- **Acreman**: Court certified class action.
Infringement of vested rights found to disclose a cause of action. Also found that retirees are vulnerable because they can no longer bargain with employer.
Court ignored the need to have proof (types of communications) provided by individual class members.



Update on Retiree Benefit Litigation

- *Bennett* appears to be a move away from *Dayco*, permitting employers to reduce retiree benefits in certain circumstances.
- This is an evolving area of the law. As such, it is very difficult to formulate rules/guiding principles.

QUESTIONS