

Pension sponsors advised to cover fiduciary liability

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CALGARY, Alberta — Canadian pension plans have become a growing source of litigation, making good risk management, including a thorough review of fiduciary liability insurance policies, a priority for Canadian risk managers.

The litigation that ensues over alleged breaches of fiduciary duty in the management of pension plans often takes the form of class actions seeking millions of dollars, said Donald McGarvey, an Edmonton, Alberta-based partner with McLennan Ross L.L.P., who specializes in commercial litigation and insurance. “The class action lawsuit is absolutely tailor-made for pension disputes,” he said during the 31st annual Canadian Risk & Insurance Management Society Inc. conference in Calgary, Alberta.

Risk managers should be concerned about the potential for lawsuits related to pension plans because of a number of factors, including the aging of the population, which is creating more potential plaintiffs; the substantial amount of money at stake in pension funds; and the increasing sophistication and knowledge of plaintiffs scrutinizing all aspects of the administration of the pension plan, Mr. McGarvey said.

Uncertainty over the rules for managing pension plans is a key emerging issue in the fiduciary liability area, with several court decisions over the last few years contributing to the uncertainty and the potential exposures for plan sponsors.

The Supreme Court of Canada’s June ruling in *Rogers Communications Inc. vs. Buschau*, which said

a common-law rule governing traditional trusts could not be invoked to force the termination of a trust holding the assets of a pension plan, was generally seen as favorable to sponsors because of the court’s recognition that judges have to be careful in applying common-law principles governing trusts to pension plans (*BI*, July 10). The decision, though, likely will result in further litigation over whether other areas of common law are also subordinate to pension legislation, Mr. McGarvey said. “When you don’t know what the rules of the game are, you’re more likely to breach them,” he said.

Another key legal question for plan sponsors is whether they can pay expenses from the pension fund, a common practice that became the basis of an adverse *Match* ruling by an Ontario court in *Nolan vs. Superintendent of Financial Institutions and Remy (Canada) Inc.* (*BI*, July 10) “This has left us in a state of flux,” Mr. McGarvey said.

Lawsuit Risk Rises

Employers are also grappling with what changes they can make to their pension plans if they act in the capacity of a plan sponsor rather than as a fiduciary of the plan—a question the Quebec Court of Appeal addressed in a case involving Montreal-based Hydro-Quebec in *Provincial Assn. of Hydro-Quebec Retirees vs. Hydro-Quebec* (*BI*, April 18, 2005).

Due to the growing legal exposures, risk managers should purchase fiduciary liability insurance Mr. McGarvey said.

Fiduciary liability insurance protects fiduciaries and the company itself for breaches of fiduciary duty and errors in the administration of the company’s employee benefit plans, said Murn Meyrick, vp of the executive risk practice of Willis Risk Solutions in Toronto.

For defined benefit plans, some alleged breaches of fiduciary duty that, barring exclusions, might be covered in the fiduciary policy are the taking of illegal contribution holidays, the wrongful payment of

expenses from the fund, negligent investment decisions, claims that certain beneficiaries were treated more favorably than others and surplus entitlement claims, Ms. Meyrick said. In some situations, the policies may exclude the actual losses caused by these events, but may still cover the defense costs, she rested

Lawsuits challenging decisions that plan sponsors make about surplus funds are considered to be a key area of risk, particularly in view of the Supreme Court's decision in *Monsanto Canada Inc. vs. Ontario (Superintendent of Financial Services)*, which required the company to distribute a portion of the surplus of a pension plan that was partially wound-up (*BI*, Aug. 9, 2004).

"We're by no means finished with surplus entitlement," Ms. Meyrick said.

Although lawsuits involving defined contribution pension plans have yet to be tried in Canada, Ms. Meyrick said she expects to see these types of lawsuits in the future. For defined contribution plans, the fiduciary liability policy may provide coverage for claims related to the selection and monitoring of service providers and the diversity of investment options, she said. Plan sponsors of defined contribution plans have to give their employees enough choice of investment options and must strike the right balance in offering education while not offering advice, Ms. Meyrick said.

A key consideration for defined contribution plan sponsors is that they still have fiduciary duties, even if they delegate the management of the plan to a third party. The belief that sponsors can contract out their liability is a "grave misconception," Ms. Meyrick said.

The plan sponsor has the ultimate responsibility to monitor, rate and confirm the quality of the performance of the service provider and may be sued if the provider does not perform up to expectations, she said

An important risk management step for plan fiduciaries is ensuring that the pension plan is governed properly, with fiduciaries able to turn to a set of regulatory guidelines that codify the responsibilities of Canadian employers with defined contribution pension plans that allow participants to make investment decisions (*BI*, Dec. 19, 2005). These guidelines have widespread industry and regulatory support and address key issues related to defined contribution plans, said Adam Briklyn, senior vp, financial tines, for Toronto-based Executive Risk Services Ltd.

Shop Early

Buyers should start shopping for fiduciary liability coverage early because there is so much pressure put on them with regard to other lines of business that the fiduciary coverage may be overlooked and they may not receive the coverage they want, he said. Risk managers should, for example, check if the fiduciary liability policy has an *Insured vs. insured* exclusion—a directors and officers policy exclusion that should not be in a fiduciary liability policy, Mr. Briklyn said.

When reviewing coverage options, risk managers should keep in mind that fiduciary liability policies are negotiable. "Don't feel as if you have to take whatever is handed to you," Ms. Meyrick said.

The session was moderated by Steve van Halst, director of insurance and claims-risk management Burnaby, British Columbia-based TELUS Corp.

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