LAWSON LUNDELL LLP

BARRISTERS & SOLICITORS

PENSION & BENEFITS LAW BRIEFING NOTE

November 2005

WESTERN CANADIAN BUSINESS LAW

Members of the Pension & Employee Benefits Law Group

VANCOUVER

Kenneth Burns
604.631.9286
403.218.7521

Murray T. A. Campbell
604.631.9187

Lisa Chamzuk
604.631.6732

John C. Kleefeld
604.631.9146

Michael Klose
604.631.6797

HEMBRUFF V. OMERS: ONTARIO COURT OF APPEAL REJECTS NOTION OF A DUTY TO DISCLOSE POTENTIAL PENSION PLAN CHANGES

By John C. Kleefeld

Overview

On November 1, 2005, the Ontario Court of Appeal held that there is no legal requirement to disclose pension plan changes under consideration, as opposed to changes that are finalized. In so holding, it reversed the March 2004 trial decision in *Hembruff v. Ontario Municipal Employees Retirement Board*, which decided that a plan administrator negligently, and in breach of its fiduciary duty, failed to tell members of potential enhancements to a plan's early retirement provisions. The Court of Appeal also reversed the trial award of over $800,000 to six plan members who had retired early and taken commuted value payments shortly before the changes took effect, leaving them unable to take advantage of the enhancements. The Court held that failure to disclose accurate and complete information about *existing* benefits could lead to such outcomes, but that the same principle does not apply to *potential* benefit enhancements, which are speculative until approved. The decision gives important guidance on the law on communicating pension information to plan members.

Background to the Case

The case concerns the Ontario Municipal Employees Retirement System (OMERS) and eight police officers who were plan members. OMERS is one of Canada's largest pension plans, serving over 300,000 members and 900 employers. It is a statutory defined benefit plan, administered by the OMERS Board pursuant to the *OMERS Act* and *Regulation*. Plan changes are made mostly by regulation.

By 1997, the plan had a significant surplus, approaching the point at which the *Income Tax Act* would have required employers to stop contributing. Under the OMERS plan, when employer contributions cease, so do employee contributions. The Board developed a five-year "surplus management" strategy that included contribution reductions and benefit enhancements. The strategy was implemented, with government passing the enhancements in late 1997.

By March 1998, though, a preliminary actuarial report indicated that the surplus was growing faster than expected, and the Board anticipated having to take further action. That anticipation was confirmed by the final actuarial valuation in April 1998, which showed a substantial growth rate in the surplus. In May and June 1998, the Board consulted with stakeholders and sent members an update informing them that a one-year contribution holiday would start in August 1998. The update also told members that the Board expected to recommend more measures to government in November 1998. In a further update in November 1998, the Board outlined the recommendations it had made, including an early retirement formula and enhanced survivor benefits. The government accepted the recommendations in a regulation passed in May 1999 and made retroactively effective to January 1, 1999.

While this was going on, Mr. Hembruff and some other employees of the Toronto Police Services Board took early retirement to pursue other employment opportunities. They chose to cash out, rather than defer, their pension entitlements. Eight of them—the plaintiffs—received their commuted value payments in 1998, while four non-plaintiffs who resigned in 1998 but whose entitlements were processed in early 1999 received additional termination benefits due to the pension plan changes. The plaintiffs said that had OMERS told them of the impending changes, they would have postponed their retirements.

What the Trial Court Did

Justice Frances Kitely held that OMERS had a duty to tell members in advance of potential plan changes so they could make informed decisions, and that OMERS had breached this duty with respect to six of the plaintiffs. She focused on when the duty arose, ruling that it was triggered by receipt of the final actuarial report in April 1998, and that the Board's duty was to convey that information before the police officers received their commuted value payments. One of those officers got his payment the same day the Board received the report, and the Court said it would be unreasonable to expect "instantaneous communication." Thus that officer, and another who had received his cheque a week prior, did not succeed at trial. The other six, though, who either resigned or received their payments after April 1998, were awarded damages in the amount of the additional benefits they would have obtained had they postponed retirement. The OMERS Board appealed to the Ontario Court of Appeal.

What the Court of Appeal Did

The Court of Appeal's judgment was written by Justice Eileen Gillese, former law professor and dean and former chair of Ontario's Pension Commission. Justice Gillese first analyzed the duty of care in negligent misrepresentation, which requires a "special relationship" between plaintiff and defendant that creates a *prima facie* duty of care, and no policy considerations, such as indeterminate liability, that would negate its existence. The Board argued there could be no duty in relation to information on potential changes, or that it was negated by policy considerations. Justice Gillese disagreed, saying it "seems beyond dispute that the Board would reasonably foresee that plan members would rely upon the pension information that it gives to them and that . . . such reliance is reasonable." Rather, the nature of the information is relevant to whether a representation is untrue, inaccurate or misleading, and whether it is carelessly made. On this

point, said the Court, failure to convey accurate and complete information about a plan's *existing* terms can be an untrue, inaccurate or misleading representation, but information on its *potential* terms is speculative, so saying nothing about them cannot support a misrepresentation claim. In other words, a crucial element of the tort of negligent misrepresentation—inaccuracy or untruth of the information—was missing in the case.

The Court next analyzed the claim for breach of fiduciary duty. The plaintiffs argued that the Board's fiduciary obligations to members required it to disclose plan amendments under consideration, particularly those that could affect members facing career decisions like retirement. However, the Court held that the only disclosure obligation was that set out in Ontario's *Pension Benefits Act*, which provides for a statutory notice period for approved amendments and a 45-day advance notice period for amendments that would reduce pension benefits. Since the enhancements did not reduce any benefits, the advance notice period did not apply. Moreover, Justice Gillese said that there were good reasons not to impose a positive obligation to disclose potential amendments, particularly in a large plan like OMERS with multiple constituencies to take into account:

> Imposition of a positive obligation to disclose plan changes under consideration would, in my view, result in an unmanageable burden being placed on the Board. Throughout . . . 1998, the Board discussed possible surplus management options at every meeting and consultation. It was a dynamic process, with options being considered and rejected and then considered again. The magnitude of the process can only be understood in context. OMERS has multiple constituencies: 300,000 members (active, deferred and retired), and 900 employers, all of whom had different interests and to whom different things might be material at different times, depending on their individual situations.
>
> In those circumstances, it is hard to conceive of how the Board could have met an obligation to disclose potential plan changes . . . . How seriously must a change be under consideration in order to trigger the obligation? What information would be sufficient to meet the obligation, given the breadth of the constituencies, member's particular circumstances, the volume of options being considered and the dynamic nature of the surplus management process? When and how would the information have to be disseminated in order to satisfy such an obligation? These difficulties are not illusory as the facts themselves show. Had the Board disclosed the potential benefit enhancement in the summer of 1998, when it appeared likely that it would be recommended, but not disclosed the [commuted value payment] withdrawal option, which was far less likely to be recommended, the information would have been incomplete and misleading as far as the respondents are concerned.

The Court went on to say that a broad disclosure obligation would thus put a plan administrator in an "invidious position" if potential changes were announced and then discarded, because some members may have made decisions to their detriment in reliance on the earlier announcements.

Finally, the Court analyzed another closely related claim—that the Board failed to treat members fairly and equitably. This claim arose because of the four non-plaintiffs who got additional benefits. They resigned in the fall of 1998, but did not submit their election forms until late 1998 or early 1999, and did not get their commuted value payments until January or February 1999. Although the amendments removed this option for members in the position of the non-plaintiffs, the Board concluded that it could not take away their rights because they were still members of the plan as of January 1, 1999.

In the face of this, the plaintiffs had alleged, and Justice Kitely had held, that the Board failed to establish transition measures that would treat all members fairly and recognize their various stages of decision-making. The Court of Appeal, though, said that *any* effective date necessarily creates a dividing line, with some benefiting and others not, and that had the Board in November 1998 recommended the amendments without a fixed date, the effective date would have been the enactment date, May 5, 1999. The Court noted that under this effective date, the plaintiffs would not have been entitled to the additional benefits (nor would the non-plaintiffs), and that recommending a fixed date "removed the irrationality of an effective date determined solely by the government's timing for enacting changes." Justice Gillese also noted that, to benefit the plaintiffs, some of whom resigned in early 1998, the effective date would have had to be made significantly earlier, likely at a significant cost to the plan and the members who remained in it, which in itself may have constituted a breach of its duty to treat the OMERS membership fairly and equitably.

Conclusion and Comment

The Court of Appeal's decision in *Hembruff* should assuage many of the concerns voiced by pension administrators after last year's trial judgment. Not only did the Court refuse to impose a disclosure obligation in respect of pension plan changes that are merely under consideration, it implicitly acknowledged an administrator's discretion to distribute benefits in the way it sees fit, as long as it exercises that discretion reasonably. On this point, see also our June 2005 briefing note on the B.C. case of *Neville v. Wynne.*

However, the Court's decision is no recipe for complacency. In particular, its threshold holding—that it can be assumed that plan members will reasonably rely on a plan administrator's communication of pension plan information—can be contrasted with case law which holds that some evidence of reliance on communications extrinsic to the formal plan documents must be adduced in order for members to be able to rely on the communications as a source of obligation on the part of an employer or plan administrator. *Hembruff* suggests that this area of law continues to evolve, and that pension communications will be a field of increasing importance.

For a copy of the case or information on its application to your circumstances, contact Murray Campbell, head of Lawson Lundell LLP's Pension and Employee Benefits Group, at (604) 631-9187 (mcampbell@lawsonlundell.com), or John Kleefeld at (604) 631-9146 (jkleefeld@lawsonlundell.com).

VANCOUVER
1600 Cathedral Place
925 West Georgia Street
Vancouver, British Columbia
Canada V6C 3L2
Telephone 604.685.3456
Facsimile 604.669.1620

CALGARY
3700, 205 – 5th Avenue SW
Bow Valley Square 2
Calgary, Alberta
Canada T2P 2V7
Telephone 403.269.6900
Facsimile 403.269.9494

YELLOWKNIFE
P.O. Box 818
4908 - 49th Street
Yellowknife, NWT
Canada X1A 2N6
Telephone 867.669.5500
Toll Free 1.888.465.7608
Facsimile 867.920.2206

The information provided in this newsletter is for general information purposes only and should not be relied on as legal advice or opinion. If you require legal advice on the information contained in this newsletter, we encourage you to contact any member of the Lawson Lundell LLP Pension & Employee Benefits Law Team listed on the front of this newsletter.

To be removed from this mailing list, please contact Lawson Lundell LLP's Marketing Manager at 604.685.3456 or genmail@lawsonlundell.com.

© Lawson Lundell LLP, 2005. All rights reserved.

Lawson Lundell LLP is a British Columbia Limited Liability Partnership.