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Bill C-501 Myths And Reality

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Most Canadians would agree that it makes sense to try to protect the retirement incomes of private-sector workers who are covered by defined-benefit pension plans. On the face of it, that's the objective behind Bill C-501, an NDP-sponsored bill that recently passed second reading in the House of Commons. The proposed legislation would force bankrupt companies to give so-called "super-priority" status to unfunded pension plan liabilities, on the grounds that this will help to ensure benefits are paid if a company goes out of business.

It sounds simple, but it isn't. And regrettably, advocates of Bill C-501 have made a number of misleading claims in support of their position, while playing down serious flaws in the legislation.

Here are some examples of the misleading claims made in support of Bill C-501:

Myth Most other developed countries already provide priority-creditor protection to defined-benefit pension plans.

Reality Very few industrialized countries offer the kind of protection envisioned by Bill C-501. Several, Canada included, provide protection for due and unpaid pension contributions in the event of bankruptcy, while others require that pensions be fully insured or guaranteed by government. In the U.S. and the U.K., companies that offer defined-benefit plans are required to contribute to funds that insure benefits up to certain limits. (Ontario has operated a similar insurance program for provincially regulated defined-benefit plans since 1980.) But those measures are in no way comparable to C-501. Germany, Ireland, the Netherlands, Portugal, the U.K. and the U.S. all have pension arrangements similar to Canada, yet in none of those countries are pension deficits given priority over all other creditors in the event of bankruptcy.

Comparisons with many other OECD countries (including Australia, Denmark, France, Italy, Poland, Spain and Sweden) are of little relevance since those countries predominantly rely on defined-contribution or state-sponsored pension plans, as opposed to the private-sector defined-benefit plans that would be affected by C-501.

Myth Granting priority-creditor status to private-sector defined benefit pension plans would have an insignificant financial impact on companies that sponsor such plans.

Reality The impact of C-501 would depend heavily on prevailing equity-market conditions and discount rates, which can drive huge swings in the value of pension funds and the size of their deficits. One of the major flaws in the bill is that it would choke off credit to companies at a time when they were most in need of it.

Under the existing provisions of the federal Companies' Creditors Arrangement Act, struggling corporations can apply for protection from creditors while they seek new financing. If C-501 passes, however, investors and lenders will have little or no incentive to provide financing to weakened companies with defined-benefit plans. They will either refuse to lend them money, or demand significantly higher premiums.

As a result, the bill would almost certainly drive into bankruptcy companies that otherwise would have been able to continue offering employment and pensions to their employees. Instead of being given a chance to restructure, such companies could be forced to liquidate.

Myth Approving C-501 is the best way for Canada's parliamentarians to help members of federally regulated defined-benefit pension plans.

Reality The federal government has already put forward a number of significant reforms that will enhance protection for plan members. Some of these measures are contained in Bill C-9, the 2010 federal budget bill; others are included among regulations announced on May 3. In the past, for example, a federally regulated company that terminated its defined-benefit plan would have been free to walk away from any pension deficit. In future, such a plan will have a claim on the assets of the corporation similar to that of any other unsecured creditor — the same level of protection currently offered to members of provincially regulated defined-benefit plans. Moreover, if the company is behind in its contributions or has failed to remit employee contributions, those amounts will be treated as "super-priority" claims.

In addition, the proposed reforms will compel plan sponsors to file actuarial updates every year, rather than every three years, a step that will reduce the size of future pension deficits by requiring that companies make supplementary payments sooner. The government is also moving to restrict the ability of employers to suspend contributions when pension plans are in surplus, and to revise the current tax rule that requires companies to halt payments when the plan is more than 110% funded.

Myth Bill C-501 will protect employees who contribute to private-sector defined-benefit plans without imposing costs on other Canadians.

Reality By giving pension deficits priority over corporate bondholders, C-501 would hurt the many millions of Canadians who invest in bonds as part of their own retirement savings. Supporters of the bill like to pretend that corporate bondholders are all rich, greedy investors and faceless corporations. In fact, most corporate bonds are held either by individual investors (who purchase bonds directly or through mutual funds) or by large public- or private-sector pension funds. In effect, C-501 would benefit one class of future retirees — those employed by federally regulated companies with defined-benefit pension plans — at the expense of many others.

Myth Bill C-501 will strengthen Canada's system of private-sector defined-benefit plans.

Reality Far from bolstering Canada's defined benefit plans, the bill would accelerate the private sector's move away from such plans. It would do so by imposing significant penalties on employers that continued to offer defined benefit plans. By raising the cost of debt and limiting its availability, the bill would damage the competitiveness of those companies and impair their ability to invest in their businesses.

Private-sector defined-benefit plans are a valuable part of today's retirement savings regime and are good for Canadian workers. But the security of pension benefits depends on financially strong plan sponsors. Bill C-501 would increase the costs of maintaining a defined-benefit pension plan in a way that ultimately would hurt the employees they exist to help, while eroding the savings of millions of other Canadians.

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