IN FACT AND IN LAW

Life and Disability Insurance and
Bankruptcy and Insolvency

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The Court of Appeal Holds that an RRSP is a Trust, and Therefore Exempt from Seizure

By Odette Jobin-Laberge

On May 10, 2005, the Court of Appeal held in Pierre Roy & Associés Inc. *v.* Bagnoud *[2005] QCCA 492, that sums transferred by Ms. Bagnoud to Investors Services Ltd. ("Investors") were a trust according to the agreements entered into between Ms. Bagnoud and Investors. This decision is one of the first interpretations by the Court of Appeal of the Supreme Court decision in* Bank of Nova Scotia *v.* Thibault.[1]

Facts

In July 1998, after her employment was terminated, Ms. Bagnoud asked that all the amounts to which she was entitled as a result of her participation in the registered retirement plan set up with her employer to be transferred to an RRSP managed by Investors.

The agreement, entitled "Retirement Savings Plan Trust", included the transfer of the sum of money representing her initial contribution to the plan to Investors, which agreed to act as trustee. The main terms are the following.

- The agreement does not provide for any payment before term, except the repayment of a premium or a payment made to the subscriber in accordance with the trust agreement.
- The trustee must keep the subscribed contributions and investment income until the plan terminates and the assets in the plan may not be assigned or withdrawn except in accordance with applicable law.

- Under the heading Investments, the trustee, at the request of the subscriber, will invest the contributions in investments eligible by law and, if the subscriber asks the trustee to invest the assets of the plan in such investment funds, he also asks it to make reasonable efforts to have redeemed as needed a sufficient number of fund units which constitute foreign property.
- The non-liability clause provides that the trustee does not assume any liability further to or in connection with investments or deposits made according to the instructions of the subscriber, except in the case of dishonesty.
- The Retirement Savings Plan Expiry clause provides that the plan may terminate any time before the end of the year in which the subscriber reaches 69 years of age or any other age prescribed by law.
- The Designation of Beneficiary clause provides that the subscriber may designate a beneficiary.

An Addendum to the Retirement Savings Plan Trust agreement was also signed. It provides that the terms of the Addendum take precedence over any other provision to the contrary in the original agreement. That addendum contains a very specific clause:

> **[Translation] "All contributions and investment income held in the retirement savings plan (the "Plan") shall be subject to the following restrictions under the Act and its regulations:**

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[1] [2004] 1 S.C.R. 758.

(a) the Plan assets may be transferred to:

(i) another locked-in registered retirement savings plan […]

(ii) a registered pension plan […]

(iii) an immediate or deferred life annuity […]

(iv) a life income fund […];

(b) the plan assets may not be subject to withdrawal, conversion or redemption but they may be paid out in the form of one or more lump sum amounts, if a doctor certifies that a physical or mental disability of the participant could considerably reduce his or her life expectancy;

(c) the plan assets may not be assigned, seized, alienated or paid in advance, except in accordance with subsection 25 (4) of the Act, and may not be the subject of an enforcement, seizure or garnishment; any transaction in breach hereof shall be null and void;

(d) the trustee shall not allow the assets to be transferred except in the cases prescribed by the Act and the regulations thereunder, and if the transferee agrees to administer the transferred funds as an annuity or deferred annuity […].”

(emphasis added by the judge)

Ms. Bagnoud had designated her spouse as revocable beneficiary on February 5, 2001 and on April 4, 2001 she made an assignment of her property.

Judgment in First Instance

Given the case law as it then existed (the Supreme Court of Canada decision in *Bank of Nova Scotia* v. *Thibault* had not yet been rendered), the trial judge agreed that there was permanent alienation of the amount deposited into the plan as, except in the case of serious illness, Ms. Bagnoud could not withdraw it except as an annuity. The trustee in bankruptcy argued that the designation of the spouse as revocable annuitant did not make the pension exempt from seizure as he was a common law spouse; the designation should have been irrevocable under article 2458 C.C.Q. The trial judge dismissed this argument and held that the designation of a common law spouse was sufficient to make article 2457 C.C.Q. apply.

Following the Superior Court judgment on the issue of the application of article 2457 C.C.Q. to a common law spouse, the Attorney General of Quebec intervened in appeal to support the trustee’s position.

Appeal Decision

Dalphond J. reiterated the principle clearly set out in *Bank of Nova Scotia* v. *Thibault* that exemption from seizure is an exception and it does not exist simply because funds are paid into an RRSP. He also held that an RRSP is a tax concept which is governed by the rules of the law of contract applicable to the vehicle used.

Is It an Annuity?

To be an annuity, it must meet the five criteria described by the Supreme Court in *Bank of Nova Scotia* v. *Thibault*:

“(i) An annuitant (a person benefiting from the annuity);

(ii) A debtor (a person who agrees to pay an annuity);

(iii) An alienation of capital for the benefit of the debtor (for example, the permanent transfer of a sum of money in cash or by periodic payments);

(iv) An obligation to pay by the debtor as of a predetermined time;

(v) Specification of a periodic amount (for example, monthly or weekly payments).”

Dalphond J. noted that there was in fact alienation of capital in favour of the trust company but that an annuity had not yet been set up as that only takes place at the end of the accrual period and the amount thus accrued may eventually be transferred to another authorized vehicle rather than an annuity. Because of this uncertainty, the contract does not yet contain a debtor, an obligation to pay or an indication of periodic amounts. He held that, as the elements required to set up an annuity were absent, it was not necessary to decide on the meaning of the word “spouse” in article 2457 C.C.Q. He noted, however, that the scope of that provision and, where applicable, its compatibility with the Quebec *Charter of human rights and freedoms*, could be debated in an appropriate case.

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Is It a Trust?

The constitution of a trust is governed by article 1260 C.C.Q. Three conditions are necessary:

> **"(i) A transfer of property from the patrimony of the settlor to another patrimony;**
>
> **(ii) The appropriation of the transferred property to a particular purpose;**
>
> **(iii) The acceptance by a trustee to hold and administer such property."**

Dalphond J. noted that the alienation criteria, the only point in common between the annuity and a trust, was met. He also held that the appropriation of capital was clearly expressed for a particular purpose, namely the purchase of an annuity or other vehicle providing security for retirement and, thirdly, that the trustee agreed to hold the amount placed in trust with it.

Prima facie there was therefore alienation of the capital and creation of a separate patrimony exempt from seizure by Ms. Bagnoud's creditors represented by the trustee in bankruptcy.

However, the trustee in bankruptcy claimed that the trustee did not have the complete administration of the amount entrusted to it as Ms. Bagnoud could indicate what investments would be made by Investors.

Dalphond J. held that the evidence showed that Ms. Bagnoud could [Translation] "*indicate a preference among the investment vehicles chosen in advance by Investors"* but that, once that preference was indicated, the trustee acted on the instructions without further intervention. The existence of this limited right to give instructions regarding investments is compatible with the existence of a true trust. To come to this conclusion, Dalphond J. quoted a comment on the *Bank of Nova Scotia* v. *Thibault* case published by John B. Claxton.[2]

Dalphond J. therefore held that, when the settlor of the trust states the nature of the authorized investments and then gives the trustee full management and administration of the amount so entrusted, the transfer to the trustee is complete and valid. The mere fact of being able to indicate a preference among the vehicles managed by Investors cannot raise doubts as to the existence of the trust or the fact that its control and administration are the prerogative of the trustee.

Comments

This decision is an excellent example of what the Supreme Court meant when it said that contracts properly drafted which meet the fundamental conditions of the legal vehicle used will be respected by the courts. The mere name retirement savings plan is not in and of itself a legal form giving any privilege whatsoever.

Furthermore, the legal regime of the trust has an important advantage in bankruptcy as the exemption from seizure, although it was stipulated here, in fact results from the very nature of a trust. The fundamental principle of a trust is to create a separate patrimony from that of the settlor so that it becomes exempt from seizure by the creditors of the settlor-debtor as it no longer belongs to him.

With respect to the application of the articles of the *Civil Code of Québec* regarding the designation of a beneficiary and the very quality of the beneficiary, Dalphond J. held that it was not relevant as it was not an annuity and he refused to discuss the issue of the validity of the naming of the common-law spouse under article 2457 C.C.Q.

If you have any questions on this bulletin or any other issue relating to retirement plans, please contact Ms. Odette Jobin-Laberge, Mr. Marc Talbot, Mr. Jean-Yves Simard or Ms. Evelyne Verrier.

[2] 2003, 63, Revue du Barreau, 255, p. 274, par. 34 and 35.

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