

CREDITOR PROTECTION

BARRING ENTRY

Looming law changes should help prevent creditors from seizing RRSP assets.

By Jamie Golombek

Creditor protection may soon be coming to an RRSP near you. This is great news for small business owners or professionals, such as doctors and lawyers, because when it comes to estate planning, these clients often cite the issue of creditor protection as their biggest concern.

While insurance products in most provinces already have various creditor protection benefits, whether your clients' non-insurance RRSPs are protected from creditors depends on where they reside and whether they're alive or dead. Generally, a creditor can seize a debtor's assets unless he or she is declared exempt in that province or territory.

Under the current rules, only Saskatchewan and Prince Edward Island have enacted laws to exempt non-insurance RRSPs and RRIFs from creditors while the annuitant is alive. The rules change slightly in the case of a deceased RRSP annuitant. British Columbia and P.E.I., for example, have legislation that exempts RRSPs from forming part of an estate.

Recent Case Law

Last year, two significant court decisions brought the issue of creditor protection to the forefront. The first case was the May 2004 decision of the Supreme Court of Canada in *Bank of Nova Scotia v. Thibault*, which ruled that creditors in Quebec could seize a debtor's RRSP because the terms of the

RRSP failed to meet the conditions necessary under Quebec legislation to exempt those assets from creditors.

The second case, a month later, was an Ontario Court of Appeal decision in *Amberst Crane Rentals Limited v. Arlene Clare Perring*, which upheld a lower-court decision exempting a deceased annuitant's RRSP from being seized by creditors, even though there are no laws in Ontario that specifically protect RRSPs from creditors.

Until the *Amberst Crane* case, the prevailing view from courts was that non-insurance RRSPs, in most common-law provinces, could be seized by creditors of a deceased annuitant even if the RRSP had named beneficiaries.

On June 3, 2005, however, Bill C-55 was introduced in the House of Commons. The bill, which proposes to amend the Bankruptcy and Insolvency Act (BIA) and the Companies' Creditors Arrangement Act (CCAA), among other things, will forge the way for creditor protection for all RRSPs.

The History

RRSPs were first introduced by the federal government in 1957, but the

first major development towards extending creditor protection to non-insurance RRSPs came 30 years later in Quebec. In 1987, Quebec law was changed to exempt fixed-term annuities, purchased from trust companies, from seizure on the same terms and conditions as annuities obtained from life insurers.

In 1990, the Manitoba Law Reform Commission proposed that RRSPs not form part of a deceased person's estate and not be subject to seizure by creditors during the person's lifetime. This law was not adopted, but later that year B.C. introduced a new law that stated RRSPs would not form part of the estate of a deceased annuitant and as a result, would not be available to creditors of the estate.

P.E.I. took a bold step in 1992 when it introduced the "Designation of Beneficiary under Benefit Plan Act," which said RRSPs could not form part of the estate and therefore could be free from the claims of estate creditors upon death. It further provided plan assets would be exempt from seizure during the annuitant's lifetime.

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In 1998, the Uniform Law Commission of Canada issued a report calling for all RRSPs to be exempt from creditors' claims. Two years later, the Superintendent of Bankruptcy created the Personal Insolvency Task Force to consider changes to the Bankruptcy and Insolvency Act. In 2002, the Task Force issued its final report recommending RRSPs be exempt from creditors on bankruptcy. That same year, Saskatchewan introduced a major piece of legislation which specifically exempts plan assets from seizure by creditors.

Last year, the Alberta Law Reform Institute released two reports calling for RRSPs to be exempt from seizure by creditors during the annuitant's lifetime and to be excluded from claims of estate creditors upon death. Legislation in Alberta has not yet been introduced.

In November 2003, the Senate Committee on Banking, Trade and Commerce released a comprehensive report entitled "Debtors and Creditors Sharing the Burden," that concluded RRSPs should be exempt from seizure in bankruptcy, subject to several conditions. This report formed the basis of Bill C-55, the 2005 draft legislation in which RRSP assets would be exempt from creditors upon bankruptcy—other than contributions made within 12 months of bankruptcy.

Interestingly, the report also proposed to exempt funds in an RESP from seizure in bankruptcy, but this recommendation didn't make it into the draft legislation released in June.

New Draft Legislation

The introduction of Bill C-55 caught some legal experts by surprise. It was "unexpected, although we were aware that significant amendments to Canadian insolvency legislation were on the horizon," says insolvency expert Natasha

MacParland, a lawyer and partner with Davies Ward Phillips & Vineberg in Toronto, who has been involved in various industry consultations on amendments to the BIA and CCAA.

Currently, many life insurance-based RRSP products as well as employer-sponsored RPPs enjoy exemptions from being liquidated upon a personal bankruptcy, while regular RRSPs can be liquidated for the benefit of creditors. "There is incongruous treatment between people whose employers force them to save for retirement versus those who save on their own," says MacParland.

If enacted, the new proposal would exempt all RRSPs and RRIFs from being liquidated on behalf of creditors upon bankruptcy and put them on the same grounds as insurance RRSPs and RPPs. "It creates a level playing field," says J.P. Bernier, vice-president and general counsel with the Canadian Life and Health Insurance Association.

Note that the new legislation doesn't mean that once passed you can make a massive RRSP contribution on one day, declare bankruptcy the next and pull all the money out a week later. There are several conditions being contemplated to prevent that from happening.

First, the draft bill proposes RRSP contributions made in the last 12 months prior to bankruptcy will not be exempt from seizure. Second, while not in the bill itself, the seizure exemption would only apply if the individual "locks in" his RRSP. No details have been provided as to the form of this locking-in, but it may very well be similar to the current locking-in rules for monies transferred from registered pension plans. These rules stipulate annual maximum withdrawal rates based on age.

Finally, there will likely be a cap on the exempted amount, which would be tied to the bankrupt person's age and the maximum RRSP contribution limit

in the year of bankruptcy. This would let older Canadians protect more of their savings than younger people.

Protecting RRSPs from seizure is consistent with the public policy objective of helping Canadians save for retirement, evidenced by the tax assistance provided to such savings vehicles inherent in our tax system. This is especially important to employees who cannot participate in an employer-sponsored pension plan and for the self-employed, whether they are business owners or other professionals. In fact, professionals, especially doctors, have often been the primary target of aggressive marketing by some life insurance advisors who heavily promote the creditor-protection benefits of segregated funds and other life insurance products.

This new legislation would also bring RRSPs in line with their U.S. counterparts: individual retirement accounts (IRAs). In a unanimous U.S. Supreme Court decision in April of this year, the U.S.'s highest court ruled that creditors could not seize IRAs in bankruptcy proceedings.

The bill received second reading on October 6th and has been referred to a committee, at which point further submissions and consultations will take place. The Investment Funds Institute of Canada has already indicated it will be joining with other lobby groups to ask that the bill's reach be extended further to allow RRSP exemption from creditors not just upon a bankruptcy.

Even if no changes are made, the ball is rolling with Bill C-55 and it's likely just a matter of time before all RRSPs and RRIFs are afforded similar creditor-protection treatment as other products. AE

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