

PENSION ENTITLEMENTS AND EQUALIZATION **ENTITLEMENTS ON BANKRUPTCY**

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Introduction

Recently it was suggested to Pension Valuers of Canada that, on bankruptcy, a person's pension plan entitlements no longer enter into the equalization calculation. In actual fact the Pension Benefits Standards Act (Canada) and the Pension Benefits Act (Ontario) both provide that no pension benefit may be assigned, charged, anticipated or given as security. They are exempt from execution, seizure or attachment. A leading bankruptcy trustee informs us that these sections make it impossible for the trustee to seize or otherwise deal with a bankrupt's pension plan entitlements. Based on this it is obvious that a person's pension plan is not affected when he declares bankruptcy, thereby leaving it as an asset that is shareable on marriage breakdown, providing the bankruptcy occurred prior to the separation date. Of course if the separation date was before the bankruptcy, it could be argued that the debt created by the equalization has been extinguished by the bankruptcy. We will explain all of this in a little more detail, (as the matter seems to arise frequently).

In Ontario, the timing of the bankruptcy, the discharge and the date of separation can be extremely important. As explained earlier in this book, on separation each party to the marriage is required to value and list his assets and liabilities. The Family Law Act then requires the party with the higher value of net assets to make an equalization payment to the party with the lower value of net assets equal to one-half of the difference. This equalization requirement creates a liability for one party and an asset for the other which comes into existence on the separation.

Of course the act of declaring bankruptcy, and the subsequent discharge therefrom, wipes out all of a person's assets and liabilities, other than their pension plan and certain other exempt assets.

The following examples will explain what happens in the equalization if one or both parties become bankrupt.

Examples:

Let's assume that we are dealing with the different timing possibilities for Mr. & Mrs. A. In each case Mr. A is the only one who has a pension and his net assets for equalization purposes are higher in value than the net assets of Mrs. A. Assume that Mr. A declares bankruptcy, then at a later date, separates from Mrs. A. The act of declaring bankruptcy wipes out all of Mr. A's assets and liabilities except for his pension.

His subsequent separation from Mrs. A. creates an equalization liability for him and an asset for her. This may work to Mrs. A's advantage since all of Mr. A's liabilities will have been wiped out on the bankruptcy leaving him with just his pension, and therefore his net assets may be higher. It has been confirmed by our legal sources that Mrs. A. will be able to recover the equalization payment from Mr. A in this example.

Now, instead of assuming that Mr. A declares bankruptcy **before** the date of separation, let us assume that Mr. A separates from Mrs. A first, and then later (before making the equalization payment) declares bankruptcy. We understand from our legal sources that this could wipe out Mrs. A's equalization right as all of the liabilities of Mr. A would be extinguished on the bankruptcy before the equalization payment is made. In this case it may be very important for Mrs. A to object to Mr. A's discharge. In the case of Patrick Gould in the Ontario Court General Division in Kenora, Ontario, Mr. Justice Gerald F. Kinsmen denied absolute discharge to Mr. Gould when his wife was his only creditor and the debt arose from the equalization process.

Now let's look at Mrs. A's position in both of these situations. Again, as in the first example above, assume that Mr. A. declares bankruptcy, then separates from Mrs. A. However, in this case, let's assume Mrs. A also declares bankruptcy before the date of separation. Since the equalization payment requirement arises on the date of separation, and Mrs. A has declared bankruptcy before that time, she should still have her equalization rights.

Now in another example assume that Mr. A declares bankruptcy then at a latter date Mr. & Mrs. A. separate. At still a later date Mrs. A declares bankruptcy before completing the equalization. In this situation our legal advisors tell us that Mrs. A's right to the equalization payment would pass to her trustee and her creditors.

For a more complete explanation of all of the above we recommend that you refer to *Bankruptcy and Family Law* by Robert A. Klotz available from Carswell. We also recommend that you refer to the reported court case of Charlotte Maureen Balyk and Steven Andrew Theodore Balyk¹ where the judge does an excellent job of explaining the relationship between the Family Law Act and the Bankruptcy Act. In that case, Wright J. gave the following useful explanations:

The parties separated in March of 1989. These proceedings were initiated in, I believe, February of 1990. The husband made an assignment in bankruptcy on June 29th, 1993. At the present time he is undischarged but his discharge is scheduled for March 29, 1994, a date which is approximately two and one half weeks hence. In effect, there is little property. In effect, the parties, having realized this, have proceeded on the basis that the debts of the husband and his other contingent liabilities, as defined in the *Family Law Act*, equal his other property, and that we should approach the equalization on the basis that the husband has one asset, that is, his pension, and no liabilities, and that the wife has no property or no assets and no liabilities. In effect, the parties say, let us treat the husband's

¹ *Balyk v. Balyk* (1994) 3 R.F.L. (4th) 282, 113 D.L.R. (4th) 719

pension as though it were the only asset for equalization purposes and proceed. Doing this, the parties agree that the pension value itself is some \$8,300, which, under this scheme, would mean that the wife has an entitlement of \$4,150.

What makes this case extremely important for the people of Ontario is the fact that the husband makes two submissions. In the first place, he submits that all proceedings against the bankrupt are stayed by virtue of section 69.4 of the *Bankruptcy Act*, and that until the wife obtains leave of this court sitting in bankruptcy to proceed, her claim against him in this respect is stayed. The second point made by the husband is that the wife has no claim against the husband other than a claim for a simple debt based upon an amount determined by the process of equalization. As such, she has a claim provable in bankruptcy and that her remedy simply is to make a claim in bankruptcy and take a share of whatever dividends may be declared by the trustee.

The wife submits that she is in the position of a secured creditor and that she is entitled to proceed without reference to the bankruptcy court. She submits that she has an interest in this pension and that she is in the same position as a secured creditor who is entitled to proceed to enforce his or her security without reference to the trustee in bankruptcy. The wife submits that she differs from an ordinary trade creditor in that the ordinary trade creditor cannot look to the pension for payment of the debt owing to it. She submits that in her case, the quantum of the debt is determined with reference to the pension and that the pension is an integral part of the ascertainment of net family property, of its equalization, and, in this case, of its payment.

The wife directs my attention, in particular, to section 9 of the *Family Law Act* and the powers given therein to the court to impose a charge on property for the performance of an obligation imposed by the order awarding an equalization of net family property under the Act.

Where such an order is made prior to the assignment in bankruptcy, I have no doubt that the property affected then passes to the trustee in bankruptcy subject to the charge, and the rights of the claiming spouse are protected. That is not our case. Generally speaking, an issue does not arise with respect to the charging of property after an assignment in bankruptcy because, generally speaking, there is no longer any property in the hands of the husband upon which such a charge might operate. This is an exception to that general rule. In this case we have an item of property which survives the bankruptcy. The wife submits that the interest of the trustee in bankruptcy is unaffected by these proceedings because the trustee had no claim on the pension, it being exempt in any event.

Dealing first of all with the procedural matter. With some trepidation, I accept that the case of *DiMichele v. DiMichele* (1981), 14 A.C.W.S. (2d) 411 [reported at 37 O.R. (2d) 314], a decision of the Ontario High Court under the former *Family Law Reform Act, 1978* still applies. In that case the court held that the leave of the court

in bankruptcy to proceed with respect to *Family Law Reform Act, 1978* matters which had been initiated prior to the husband's bankruptcy was unnecessary but that the trustee should be served.

I am prepared to accept, for our purposes today, that it was unnecessary for the wife to obtain leave of the bankruptcy court to continue these proceedings. This, then, brings us to the substantive issue.

The wife also refers me to the case of *Boe v. Boe*, a decision of the Saskatchewan Queen's Bench (1987), 6 R.F.L. (3d) 383. In that case, proceedings under the Saskatchewan *Matrimonial Property Act* had been commenced and had come to judgment, and an award of \$100,000 payable in instalments had been made to the wife. The judgment had been directed to be registered against the lands registered in the husband's name to secure payment. Subsequently, before paying the judgment, the husband made an assignment in bankruptcy. In that case it was held that the wife had a proprietary interest in the realty, and to this extent she was cured and the trustee took subject to her security.

I begin with the proposition that the family property regime which has been in effect in Ontario since the implementation of the *Family Law Act* in 1986 is one which is somewhat unique in Canada. Most, if not all, of the other common law provinces of Canada enacted family property legislation which implemented a family assets regime. Ontario led the way with the *Family Law Reform Act* in 1978. Those Acts, generally speaking, provided a class of property said in the case of the Ontario statute to constitute "family assets." Now, as Madam Justice Boland pointed out in *Stoimenov v. Stoimenov* (1982), 40 O.R. (2d) 69 (H.C.), those Acts did not confer upon a non-titled spouse an interest in the asset. What most of these statutes do is confer upon a claimant a right to claim an interest in the asset. What most of these statutes do is confer upon the claimant a right to claim an interest in the asset. Upon adjudication, the court defines the interest of the spouse. In *Re Collins* (1981), 12 A.C.W.S. (2d) 215 [[1982] W.D.F.L. 152], Mr. Justice Steele, in the context of a bankruptcy, pointed out that under a family assets regime, and, in particular, the *Family Law Reform Act* of Ontario, section 4 of that Act gave a right to both spouses in the family assets regardless of whose name the property was registered in. He pointed out that these rights had to be determined before the rights of the trustee in bankruptcy could be determined in the bankruptcy court. He pointed out that the *Family Law Reform Act* provided not only for an equal division of the assets but also provided that the court could make a division in shares that were not equal. Accordingly, it was his opinion that, at the time of the bankruptcy, there was no firm debt owing or any firm determination as to which spouse owned which particular assets. In his opinion, these issues were to be determined by the regular courts before proceedings continued in the bankruptcy court.

Generally speaking, under the family assets regimes in the provinces other than Ontario, the parties remain separate as to property. However, upon the occurrence of certain specified events, one of which invariably is the separation of the parties,

certain rights arise. In the case of Saskatchewan, the right was to have either the property divided in specie between the parties or its value divided between the parties. In *Boe*, that in fact had been done, and the value had been divided and the wife's interest secured. It accordingly survived any assignment made by the husband. In *Re Roussel* (1981), 37 C.B.R. (N.S.) 262 (Ont. S.C.), Mr. Justice Hollingworth was faced with a case involving parties who had separated in 1977 and who had been divorced in December of 1978. The matrimonial home, the title to which was in the name of the husband alone, had been sold by the husband's trustee in bankruptcy in February of 1981. The trustee then applied to the court for advice as to the disposition of the proceeds. The court held that the prerequisites of the then section 4(1) of the *Family Law Reform Act, 1978* had been met, that the wife's interests had crystallized prior to the bankruptcy, and that the wife was entitled to 50 per cent of the funds realized upon the sale of that matrimonial home. In *Phillips v. Phillips* (1982), 30 R.F.L. (2d) 353 (Ont. Co. Ct.), and, in particular, at page 358, 359, His Honour Judge Mossop, as he then was, distinguished the case of *Re Collins*, to which I have already referred, on the ground that in that in the *Collins's* case, the spouses had separated six months before the assignment in bankruptcy so that there had been, as he called it [at p. 358], a "triggering effect" under section 4, which was lacking in the case before him. My recollection is that in *Phillips* the separation, or the crystallizing event, had occurred subsequent to the assignment in bankruptcy. Another case on point is *Re Radovini* (1981), 22 R.F.L. (2d) 275 (Ont. S.C.), also reported in 37 C.B.R. (N.S.) 264. In that case the matrimonial home was registered in the name of the husband. It was sold and the proceeds were held by the husband's trustee in bankruptcy. The wife argued that the purpose of the *Family Law Reform Act, 1978* was to protect her and that she should be entitled to one half of the proceeds. Now, in that case, the court held that before the wife could take any interest in the matrimonial asset, one of the prerequisites in section 4(1) of the then *Family Law Reform Act, 1978* must exist. In *Radovini*, the parties in fact had not separated. The wife was held to have no inchoate right, pursuant to the *Family Law Reform Act, 1978*, to an interest in the matrimonial home.

The regime implemented by the *Family Law Act* of 1986 was dramatically different from the regime in place under the *Family Law Reform Act, 1978* and continues to be dramatically different to most, if not all, of the family property regimes in the other common law provinces of Canada. The legislature, in its wisdom, chose to abandon a family assets regime and to substitute in its place a regime which made the claimant spouse a simple creditor of the other party. The regime as implemented by the *Family Law Act* simply provides that the net family property of each party is to be determined in accordance with the provisions of that Act, and that subject to specified considerations, the value of the net family property of each party is to be equalized by an award of money from one party to the other. I am not overlooking the provision already referred to contained in section 9 of the Act, which provides for payment by means of security against assets, and, indeed, for the transfer of assets in specie in realization of the judgment. The fact, however, remains that under the present regime or the existing regime in Ontario, the

claiming spouse is simply an unsecured creditor. She or he has, in my opinion, a claim provable under the provisions of the federal *Bankruptcy Act*. While this may seem to be harsh in cases such as this, I cannot torture the law to fit the hard case. It would be a simple matter for the legislature to revert to a family assets regime and it would be an equally simple matter for the federal government to provide an exception for family asset disputes in the *Bankruptcy Act*. Neither has been done. I must apply the law as I perceive it to be.

The arguments by the wife that the pension constitutes a special type of property fails. Notwithstanding that the value of the pension is a factor to be considered in determining the husband's net family property, the pension itself is not exigible, nor is the court in a position to make any meaningful charging order against it. Under the circumstances, I must hold that the wife, while she is a creditor in the amount of \$4,150, is left to her remedies in the bankruptcy court to collect that sum. It may be that she may be able to oppose an application for discharge on terms, and she may have other remedies under the *Bankruptcy Act*, but these are not of concern today...

For reasons delivered, judgment against the husband for equalization in the amount of \$4,150, declaration that this constitutes a "claim provable in bankruptcy". Husband to pay costs as on a uncontested divorce, being \$400, plus those disbursements. Access as agreed.

In commenting on recent court cases involving Bankruptcy and Family Law, the 2000 *Annual Review of Family Law* by James G. McLeod and Alfred A. Mamo says,

A spouse's bankruptcy causes a number of problems in the context of equalization proceedings. Bankruptcy should not be used for the primary purpose of evading a debt owing to a spouse: *Re Richardson* (1998), 41 R.F.L. (4th) 141, 5 C.B.R. (4th) 280 (Ont. Bkcty.)(spousal debt not akin to commercial debt); *Coathup v. Coathup* 2000 CarswellOnt. 247 (bankruptcy not a vehicle to wipe out equalization rights); *Re Kostiuik* 2000 BCSC 400 (B.C.S.C.)(nature of matrimonial property regime relevant). A court may annul a bankruptcy as an abuse of process where a spouse has made himself insolvent by transferring away property in violation of court orders: *Stasiuk v. Stasiuk* (1999), 46 R.F.L. (4th) 382, 9 C.B.R. (4th) 182 (B.S. S.C.) [In Chambers]).

Even if a spouse is discharged from bankruptcy, he or she may retain exempt property against which the other spouse may choose to assert property rights: see *Re Gruending* (1999), 47 R.F.L. (4th) 414, 170 D.L.R. (4th) 541, 6 C.C.L.I. (3d) 1, 8 C.B.R.(4th) 246, 61 C.R.R. (2d) 338, [1999] I.L.R. I-3703, 239 A.R. 201 (Q.B.) with respect to scope of property exemption.

As well, a spouse may try to access property that is not exempt under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, by asserting that the debtor

holds the property in whole or in part on trust for her: *Cowger v. Cowger*, [1998] W.D.F.L. 1053 (N.W.T. S.C.).

Whether a person can enforce an equalization entitlement against his or her bankrupt spouse depends on the timing and nature of the property order and whether the bankrupt received an absolute discharge from bankruptcy: *Re Richardson*, [1998] W.D.F.L. 842 (Ont. Gen. Div.). A monetary judgment or entitlement will be discharged by the debtor's bankruptcy, but a property order or transfer prior to the bankruptcy should prevent the property passing to the bankrupt's trustee in bankruptcy: *Godfrey v. Godfrey* (1996), 19 R.F.L. (4th) 58 (Ont. Gen. Div.).

In *Hildebrand v. Hildebrand* (1999), 13 C.B.R. (4th) 226, 140 Man. R. (2d) 316 (Master). Master Harrison reviewed the effect of bankruptcy on a spouse's matrimonial property application and when a spouse should be allowed to continue the application with the Trustee in Bankruptcy as a party.

For other interesting and informative reading see *Bankruptcy and Family Law* by Anne-France Goldwater, which appeared in the January 1998, issue of *Family Law Quarterly*. Also refer to the following reported court cases.

- *Gough v. Gough* (1996) 92 O.A.C. 384 (Ontario Ct. of Appeal)
- *Blowes v. Blowes* (1993) 49 R.F.L. (3d) 27, 16 O.R. (3d) 318 (Ont. Ct. of Appeal)
- *Re Wale* (1996) File No. 35-063684 (Ont. Ct. Gen. Div.)
- *Re Richardson* (1998) 41 R.F.L. (4th) 141 [Ont. Ct. of Justice, Gen. Div. (In Bankruptcy)]
- *Stiles v. Stiles* (1999) 11 C.B.R. (4th) 315 (Ont. Ct. of Justice, Gen. Div.)