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IMPORTANT PROPOSED CHANGES RELEVANT TO PENSION PLANS

BY REESHA HOSEIN

The federal government has recently announced significant changes to federal pension legislation that will be relevant to many Canadian registered pension plans. The changes are particularly relevant to pension plans with members whose entitlements are governed by the federal *Pension Benefits Standards Act*. The government's description of its pension reform proposal can be found at: <http://www.fin.gc.ca/n08/09-103-eng.asp>.

The federal government is expected to implement its pension reform proposal in 2010. We have highlighted some of the proposed changes below.

Changes relevant to all Canadian defined benefit pension plans

Plan sponsors will be able to accumulate greater amounts of surplus in defined benefit pension plans in an effort to reduce the severity of future funding deficiencies. The surplus threshold under the *Income Tax Act* will now be 25% (generally calculated on the basis of liabilities on a going concern basis). Previously, plan sponsors were not allowed to make further contributions to a pension plan where a surplus of 10% existed.

Changes relevant to many Canadian pension plans

The federal government has proposed changes to modernize the pension fund investment rules. These new rules will be clearly applicable to benefits in

provinces that have directly adopted the federal investment requirements (specifically, Alberta, British Columbia, Manitoba and Saskatchewan). These new rules may apply to benefits in Ontario and Nova Scotia if these provinces modify their legislation to follow the federal changes. It is unclear how these changes will affect benefits in Québec and New Brunswick, as these jurisdictions have not adopted the federal requirements.

In summary, the proposed changes will:

- Amend the 10% concentration limit so that pension funds cannot invest more than 10% of the *market value* of the assets of the pension fund in any one entity. There will be an exception allowing pension funds to invest more than 10% in pooled funds where the employer does not exercise direct control over the pooled fund. Currently, pension funds are restricted from investing more than 10% of the *book value* of the pension fund in any one entity.
- Remove the quantitative limits in respect of Canadian resource and real property investments. The federal investment regulations currently prohibit investments of more than 5% of the value of a pension fund in one parcel of real property or Canadian resource property, investment of more than 15% of the aggregate value of the pension fund in Canadian resource properties, and finally, prohibit investment of more than 25% of the pension fund's assets in any combination of real property and Canadian resource property (note that all of the above percentages are calculated on the basis of the book value of a pension fund's assets).
- Completely prohibit an employer from direct self-investing. This would mean that an employer would not be allowed to invest any pension fund assets in its own debt or shares.

Notably, no change has been proposed to the rule that restricts pension plan sponsors from acquiring more than 30% of the voting shares of corporations. This so-called "30% rule" was the subject of intense commentary during the 2008 attempted acquisition of BCE Inc. by the

Ontario Teachers' Pension Plan. The federal government has not signalled any intent to change the 30% rule.

Changes relevant to federally registered pension plans

Below are highlights of the proposed changes to the federal pension rules that will be relevant to federally registered pension plans (as well as plans that are registered with a provincial authority, but have federally-governed members).

Relevant to all federal plan sponsors:

- Benefits will immediately vest once a member commences membership in a pension plan.
- A plan sponsor will be able to meet disclosure requirements in an electronic format, as long as the member consents. Deemed consent will not be permitted

Of particular relevance to federal defined benefit pension plan sponsors:

- A "workout scheme" is proposed to allow plan sponsors, members, and retirees of a pension plan to negotiate funding arrangements (outside of the regular funding framework) to provide relief to "distressed" companies. For example, the workout scheme would allow a plan sponsor to negotiate changes to its funding schedule for special payments.
- A plan sponsor will be required to fully fund a terminated pension plan on wind up (in equal payments over five years), and the amount required to be funded will be an unsecured debt of the plan sponsor until fully paid.
- Contribution holidays will be allowed only if the pension plan is fully funded by more than 5% on a solvency basis.
- Amendments providing for benefit improvements will not be allowed where the pension plan's solvency ratio is 0.85 or less.
- Letters of credit may be used to satisfy solvency payments up to a limit of 15% of a pension plan's assets.
- The method of calculating solvency funding requirements will change.

- Member annual statements will be required to disclose greater information regarding the funded status of the pension plan.

Of importance to federal defined contribution pension plan sponsors:

- There will be "explicit guidance" on the responsibilities of administering a defined contribution pension plan (with a view to current Capital Accumulation Plan Guidelines from the Canadian Association of Pension Supervisory Authorities).
- The requirement for a Statement of Investment Policies and Procedures (SIP & P) will be eliminated.

The proposed changes are wide-ranging and will have a significant impact on plan sponsors if they are all implemented. We will continue to provide updates as the government provides more information.

NEW DISCLOSURE RULES PROPOSED FOR FEDERALLY-REGULATED DEFINED CONTRIBUTION PENSION PLANS

BY MARY PICARD AND HEATHER DI DIO

A new disclosure policy for defined contribution registered pension plans has been proposed by the federal pension regulator. The regulator is seeking comments on the proposed guideline up to December 31, 2009. To access a complete copy of the Guideline, please visit http://www.osfi-bsif.gc.ca/osfi/index_e.aspx?ArticleID=3194. The following comments may be of interest to federally-regulated sponsors of registered pension plans, as well as other pension plan sponsors who may view the federal guideline as a prudent standard for all plans.

On September 4, 2009, the Office of the Superintendent of Financial Institutions ("OSFI") released its "Draft Disclosure Guideline for Defined Contribution Pension Plans" (the "Draft Guideline"). It sets out detailed requirements of what OSFI will expect pension plan sponsors to disclose to plan members, eligible employees and spouses as required under the *Pension Benefits Standards Act, 1985* ("PBSA") and the *Pension Benefits Standards Regulation, 1985* ("PBSR"). The purpose of the Draft Guideline is to try to ensure that plan members and former members receive appropriate information about their defined contribution pension plan.

Most plan sponsors are aware of the Canadian Association of Pension Supervisory Authorities

("CAPSA") guidelines for capital accumulation plans that were issued in 2004 (the "CAP Guidelines")ⁱ. OSFI's Draft Guideline formally approves of the CAP Guidelines, and recommends that they should be followed, along with OSFI's Guideline for Governance of Federally Regulated Pension Plansⁱⁱ.

Disclosure of information in a defined contribution pension plan to plan members, potential members, former members and member spouses is not a new issue. What is new is the amount of detail and clarification OSFI provides in the Draft Guideline regarding what information will satisfy plan sponsor requirements, specifically under section 28 of the *PBSA* and sections 22-23 of the *PBSR*. Section I of the Draft Guideline discusses at length the informational requirements of member booklets and sets out exactly what must be included in a member booklet. The Draft Guideline also emphasizes that plan members, eligible employees and spouses should be provided with knowledge about (1) investment information and decision tools, (2) expenses, fees and penalties, (3) annual statements, (4) plan amendments and (5) termination and retirement statements. It is the plan sponsor's responsibility to ensure that its pension plan complies with applicable pension standards, and that plan materials and communications adhere to the Draft Guideline after it is adopted.

All sponsors of defined contribution pension plans, whether or not federally-regulated, can apply the principles and governance directives in the Draft Guideline as a "best-practice" to follow. Once adopted, the Draft Guideline will replace the OSFI guideline entitled "Disclosure of information to pension plan members and former members" issued on March 6, 1998 with respect to defined contribution plans.

CONTACT US

If you have any questions on the federal government's pension reform proposal or if you want to know if your company's disclosure is adequate, please contact a member of our [Pensions|Benefits Group](#).

ⁱ CAP Guideline No. 3 and No. 4 are available at: <http://www.capsa-acor.org/capsa-newhome.nsf/4a5938dfa169be3285256c1a00752c5d?OpenView>.

ⁱⁱ Available at: http://www.osfi-bsif.gc.ca/app/DocRepository/1/eng/pension/guidance/govengl3_e.pdf.



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