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ONTARIO PENSION REFORM: TIME TO AMEND YOUR PENSION PLAN?

BY MARK DUNSMUIR

It's official: the Ontario government has voted to amend the Ontario *Pension Benefits Act (PBA)*. This represents the biggest overhaul of Ontario's pension legislation in more than twenty years.

On May 5, 2010, the amendments to the *PBA* were passed on third reading in the Ontario legislature ([the most recent on-line version of Bill 236 – An Act to amend the Pension Benefits Act](#)). As of May 6, 2010, these changes have not received royal assent. We expect that the necessary government assents and proclamations to make these amendments law will be forthcoming.

If you are the administrator or the employer sponsor of a pension plan registered in Ontario, or a pension plan with Ontario members, these changes will significantly affect the operation and liabilities of your pension plan.

Most pension plans will have to be amended in order to comply with the new state of pension law in Ontario.

Some of the changes could have a substantial impact on pension plan liabilities. Sponsors of defined benefit pension plans should consider whether they wish to amend their plans to avoid the new liabilities imposed by the changes.

The *PBA* reform also imposes novel obligations on administrators and sponsors that will not require pension

plan amendments. Even if no amendments are required, sponsors and administrators should make sure that they understand all of the new and expanded obligations.

A not-so-fine balance?

Early government press releases claimed that the reforms were designed to strike a balance between the interests of employers and employees. However, most of the reforms impose new obligations on employers and pension plan administrators.

Certain administrative and funding costs will increase for sponsors of defined benefit (DB) and defined contribution (DC) registered pension plans. Sponsors of DB pension plans could see their contribution obligations increase due to the extension of special early retirement benefit enhancements known as "grow-in" benefits, depending on the structure of early retirement benefits in their particular plans.

On the other hand, there are some welcome improvements in the rules regarding pension plan mergers, procedures to implement surplus sharing deals and the elimination of partial wind-ups.

The Ontario government has achieved what no provincial government has been able to achieve in the past couple of decades: a significant "clean up" of surplus and pension plan merger rules to the benefit of many stakeholders in the pension world.

Compliance amendments

The following change to the *PBA* will require amendments to most pension plans with Ontario members:

- **Immediate vesting.** As soon as Ontario employees join a pension plan, they will vest immediately. Most pension plans have a qualifying period of up to two years of membership before a member is entitled to the employer contributions made on their behalf.

Pension plans that impose a qualifying period will have to be amended to eliminate this period. Employers may still impose a two-year waiting period to join a pension plan.

Amendments to avoid new obligations

The following change to the *PBA* could significantly increase the liabilities of a pension plan with Ontario members. Sponsors of pension plans affected by these amendments should consider amending their pension plan to reduce this increased liability:

- **Grow-in benefits in DB plans will be extended.** Currently, DB pension plans which provide enriched early retirement benefits must provide a “grow-in” benefit to employee members whose age and service total at least 55, **only** if the members terminate as part of a partial or full pension plan wind-up. Typically, this expensive grow-in benefit is granted only on plant closures. Not any more. Commencing July 1, 2012, grow-in benefits must be given to all terminating members whose age and service total at least 55, regardless of whether they are terminating due to a full or partial pension plan wind-up. The only exception will be if the affected employee voluntarily resigns or is fired “wilful misconduct.” This could create a significant funding cost for sponsors of DB pension plans that have enriched early retirement benefits. The financial impact will depend on the design of the enhanced early retirement provisions in each particular pension plan.

In order to avoid this new liability, sponsors can consider amending their pension plan to remove or neutralize these enhanced early retirement benefits. If the enhanced early retirement provision is no longer in the pension plan, the new extension of grow-in will not apply.

New administrative obligations

The following changes will not require amendments to pension plans with Ontario members, but administrators and employers should be aware of them simply because they add new obligations:

- Increased employer sponsor obligations to inform pensioners and members, and a requirement to give pensioners and members greater access to pension plan oversight. All pension plan sponsors, both DB and DC, will

have to provide increased access to information for pension plan members and pensioners.

In fact, administrators will now be required to facilitate the establishment of pensioner and member oversight committees and to assist in the operation of such committees.

Although changes to the *PBA* will permit the costs of operating an oversight committee to be paid from the pension plan fund, sponsors are not required to permit this subsidization.

- **Expanded disclosure.** The first version of the government’s amendments to the *PBA* included a provision permitting sponsors to refuse to disclose certain records if the pensions regulator determined that the disclosure could be expected to prejudice the economic interests of the sponsor. The limitation on the expanded disclosure requirement has been removed; meaning sponsors and administrators may be required to hand over documents that may prejudice the sponsor’s economic interests.
- **Expanded obligations regarding notice of amendments.** Currently, an administrator is required to provide advanced notice of a pension plan amendment only to members if the amendment is adverse in nature. Changes to the *PBA* will require administrators to provide advanced notice to members for all amendments except for amendments that may be included in the regulations that will be released at a later date.
- **Phased retirement.** Although not mandatory, sponsors of DB pension plans may now provide their employees with an option to receive their pension benefit through a phased retirement option. If a sponsor wishes to provide its employees with phased retirement, amendments to the pension plan will be required

Some excellent news: a reduction in costs and administrative obligations

The following proposed changes will simplify the administration of DB and DC pension plans, and reduce costs, in certain circumstances:

- **The rules for merging or restructuring pension plans will be “clarified and simplified.”** Because the regulations have not yet been released, the potential benefits of this

amendment may be reduced if the devil proves to be in the details. If the regulations prove to be sponsor friendly, this change could be significant for employers who have been unable to proceed with pension plan mergers over the past few years due to legal challenges.

- **Surplus sharing agreements will no longer require expensive historical reviews.** If a sponsor can get the members of a terminated or partially terminated pension plan to agree to share the surplus of a pension plan, it will no longer be necessary for the sponsor to prove that it owns the surplus according to historical pension plan documents.
- **The elimination of partial pension plan wind-ups.** No partial pension plan wind-ups will be allowed, following a transition period that will end on a date to be proclaimed. This is very good news for DB and DC pension plan sponsors. The requirement to distribute surplus on partial wind-ups will disappear. The expense and delays in carrying out partial wind-ups will no longer exist and there will no longer be disputes regarding the annuitization of benefits in partial wind-up circumstances.

Unfortunately, for sponsors of DB plans, the elimination of partial pension plan wind-ups comes at the cost having to extend grow-in benefits, and provide immediate vesting as explained above.

MORE CHANGES TO FEDERAL PENSION LEGISLATION, INCLUDING PENSION INVESTMENT REQUIREMENTS APPLICABLE TO MANY CANADIAN PENSION PLANS

BY N. REESHA HOSEIN

In the most recent development in federal pension reform, the federal Department of Finance released its [proposed amendments to the Regulations to the Pension Benefits Standards Act 1985](#) (the "Regulations") for comment.

The measures included in the most recent iteration of the federal government's reform package are primarily relevant to sponsors of defined benefit pension plans, as they focus on changes to pension fund investment requirements, and the rules regarding contribution holidays and solvency funding. That being said, the changes to the pension fund investment requirements will affect many provincially regulated pension plans

which are also subject to federal investment requirements.

Please see our previous Focus on Pensions/Benefits publications for our prior discussion of the changes to federal pension standards legislation: [November 2009](#), [April 2010](#).

Changes to pension investment requirements

We note that once finalized, these changes will likely apply to pension plans registered in Alberta, British Columbia, Manitoba, Saskatchewan and Ontario, which have adopted the federal pension investment requirements.

The proposed Regulations repeal the quantitative restrictions applicable to investments in real estate and Canadian resource properties. Currently, a pension plan may not hold more than 5% of its portfolio in a single piece of real estate or Canadian resource property, total investment in real estate and Canadian resource property cannot be more than 15% of a pension plan's portfolio, and combined investment in real estate and Canadian resource property cannot constitute more than 25% of the pension plan's portfolio. The Department of Finance in its "Regulatory Impact Analysis Statement" states that this change is in response to representations from plan sponsors and service providers indicating that these quantitative limits are unduly restrictive where a general prudence requirement governs pension plan investments.

The Department of Finance confirms that it intends to implement both the previously announced change to the 10% concentration rule (i.e. presumably restricting pension funds from investing more than 10% of the **market value** instead of the current **book value** in any one investment), as well as the prohibition on investment in the shares of a sponsoring employer, in upcoming regulatory amendments.

Also noteworthy is the federal government's statement that it does not intend to remove the restriction on pension funds holding more than 30% of the voting shares in any single entity, despite representations by plan sponsor and service providers that this restriction is no longer relevant in a world where pension fund investments are held to a prudence standard. The federal government's decision to maintain this restriction is based on its view that its removal would "increase the potential for pension plans to own and operate companies".

In a nutshell, this means once the Regulations are finalized, pension plan sponsors (including sponsors of

many provincially registered pension plans) should review their statement of investment policies and procedures to determine whether changes to pension plan investments would be appropriate.

Changes to rules for contribution holidays

The proposed changes would only allow federally-regulated plan sponsors to take “contribution holidays” where the solvency ratio of a plan is greater than 1.05. Currently, where the solvency ratio of a plan is equal to 1.0 (or is “fully funded”), a contribution holiday is allowed. This change may not have a significant impact for plan sponsors recovering after the recent economic downturn, but may have greater relevance in the future as pension plans return to surplus positions.

Changes to the solvency funding rules

The amendments to the plan funding rules will change the average of solvency ratios over three years as the basis for determining minimum funding requirements. Prior to the proposed change, the Plan’s current solvency ratio is used to determine funding requirements. Solvency deficiencies will continue to be amortized over five years. Interestingly, this change to the use of an average solvency ratio will only be used for funding purposes; the current solvency ratio would still be used for purposes other than funding as required under federal pension standards legislation.

Particularly with respect to the changes in federal investment requirements, the release of this most recent round of reforms to the federal pension regulatory framework indicates that, despite the submissions of plan sponsors, reform will not go as far as plan sponsors may have hoped.

For further information on this, and the other proposed reform to federal pension standards legislation, please contact a member of our Pensions/Benefits Group.

CONTACT US

For further information, please contact a member of our [National Pensions | Benefits Group](#).



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