focus on Pensions and Benefits

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IMPORTANT POLICY DEVELOPMENTS ARISE FROM MONSANTO CASE

On August 31, 2004, the Financial Services Commission of Ontario ("FSCO") released its first policy in respect of partial wind up procedures following the Supreme Court of Canada's decision in *Monsanto Canada Inc. v. Superintendent of Financial Services ("Monsanto")*. In a statement entitled *Partial Wind Ups Post-Monsanto*, FSCO indicated the following in respect of partial wind up reports that have already been filed with FSCO:

- Where a report indicated that no surplus existed as of the partial wind up date, the filing was complete, any outstanding questions were addressed and the report was approved, then the partial wind up is considered to be complete upon distribution of the basic benefits relating to the partial wind up;
- Where the report reflected a surplus at the time of the partial wind up and approval of the report had been given by the Superintendent of Financial Services (the "Superintendent"), the partial wind up is complete once the assets attributable to the partial wind up are distributed;
- Where a report reflected a surplus as at the date of the partial wind up but no proposal to distribute the surplus was filed and the Superintendent has not approved the partial wind up report, additional filings will need to be made to deal with the surplus related to the partial wind up group. FSCO was to have sent letters which detailed the required filings to affected plan administrators by August 29, 2004. Affected plan administrators who do not receive letters are to contact FSCO at the address provided in FSCO's statement;
- Where a hearing before the Financial Services Tribunal relating to a partial wind up has been put on hold pending the Supreme Court of Canada's decision in *Monsanto*, those hearings can now proceed on the request of one of the parties.

With respect to the fourth category of partial wind ups, it should be noted that the Ministry of the Attorney General is now sending out letters to the FSCO registrar asking that all hearings that were on hold be scheduled.

FSCO is also in the process of reviewing all of its current policies concerning wind up, partial wind up and surplus and will be replacing policies shortly. The first "new" policy to be introduced will be S900-511, Application by Employer for Payment of Surplus on Partial Wind Up of a Pension Plan. It is hoped that the revised policies will give plan administrators some guidance on the many unanswered questions brought about by the decision in *Monsanto*.

If you would like to receive a copy of FSCO's August 31, 2004 statement, please call a member of the Toronto Pensions and Benefits Group or go to the FSCO website at www.fsco.gov.on.ca

FSCO'S PROPOSED INVESTMENT MONITORING MODEL FOR DEFINED BENEFIT PENSION PLANS

Pension fund investments are an area of pension administration that has received little attention from regulators. However, because of severe pension funding shortfalls created over the last number of years, which have been caused in part by the downturn in equity markets, regulators are now beginning to focus more of their attention on the financial health of registered pension plans.

For its part, FSCO implemented a monitoring program in 2000 that focused on pension plan funding. As a follow up to that program, FSCO has now released a consultation paper entitled *A Proposed Risk-Based Investment Monitoring Model for Supervising Defined Benefit Pension Plans* (the "Investment Monitoring Model") which focuses specifically on the investment of defined benefit ("DB") pension plan assets. Both the funding program introduced in 2000 and the Investment Monitoring Model represent a "risk-based" approach to the supervision of pension plans. This approach focuses on pension plans most at risk of not providing members with the benefits they have been promised under their pension plan.

In introducing the Investment Monitoring Model, FSCO's main objectives were to encourage appropriate investment conduct and processes and to promote good fund governance. The Investment Monitoring Model tries to achieve these regulatory goals through a selective review process. The first stage of this process, the "risk assessment stage", would see FSCO measure the relative risk potential of pension plans based on FSCO's predefined risk assessment criteria. This would require the collection of pension plan financial information as well as other investment information through the use of a standard form that will be completed by plan administrators. The second stage would involve an "investment review" of those plans selected in the first stage. This would entail a closer examination of the pension fund investment activities, including such things as non-compliance with investment regulations and the funded status of the pension plan. In the third and final stage, the "follow up stage", FSCO would seek resolution of any outstanding concerns identified in the first two stages. FSCO expects to implement the Investment Monitoring Model for filings made in respect of the 2004 plan year-end. Initially, the Investment Monitoring Model will only apply to DB pension plan's, since a different model would be needed for defined contribution arrangements.

To a significant degree, FSCO's risk assessment is based on certifications of investment rule compliance, including compliance with the pension plan's statement of investment policies and procedures, from the plan administrator (and the plan's auditor if the pension assets total $3 million or more). This will require plan administrators to be much more aware of the investment rules and regulations for registered pension plans and the plan administrator's fiduciary obligations in respect of pension fund assets if they are going to certify investment compliance. Since the draft certification form required by FSCO is quite detailed in respect of investment compliance, consideration should be given to specifically amending investment management agreements to ensure that third parties, such as investment managers, will not only comply with investment regulations but will also provide plan administrators with a certification of compliance.

If you would like to receive a copy of the Investment Monitoring Model provisions and the proposed compliance certificate, please contact a member of the Toronto Pensions and Benefits Group, or go to the FSCO website at www.fsco.gov.on.ca.

DOES YOUR PENSION PLAN HAVE TO BE AMENDED TO REFLECT INCREASED DEFINED BENEFIT LIMITS?

The DB limit has increased from $1722.22 in 2003 to $1833.33 in 2004 per year of service. This limit increases to $2000 in 2005, after which it will be indexed according to the average industrial wage.

Plan sponsors with plan texts that have a fixed DB benefit that does not automatically increase in accordance with increases in the tax regulations will have to amend their texts if they would like their plan members to take advantage of these higher DB limits. This past February, the Federal government introduced a draft regulation to provide relief from the requirement to report past service pension adjustments ("PSPAs") if a DB plan is amended in 2004 to provide for the increased DB limits. If the pension plan is not amended until 2005, only partial PSPA relief is available. (The PSPA rules are triggered whenever a pension plan is amended to provide a benefit improvement retroactively to a previous calendar year.) Any DB plans amended after 2005 will be subject to regular PSPA reporting.

If your DB pension plan is worded such that the DB limit rises automatically with changes in tax regulations, there is no need to make any amendments to your plan and PSPA reporting will not be required. If your company does not wish to allow plan members to enjoy the increased maximum limits (which translate into higher benefits and additional funding), then there is no need to worry about such amendments and any PSPA reporting. However, keep in mind that if there is a change of heart later (e.g. after 2004), the PSPA issues noted above will apply.

Finally, although the draft regulation has not been finalized, steps should be taken to make the amendment this year if you would like your employees to take full advantage of the increased DB limits. If you require assistance in amending your DB plan, please contact a member of the Toronto Pensions and Benefits Group.

A REMINDER ABOUT RESTRICTIONS ON COMMUTED VALUE TRANSFERS - ONTARIO

Administrators of Ontario registered pension plans should be mindful of the restrictions on the transfer of pension benefit commuted values contained in the Ontario *Pension Benefits Act* Regulations ("PBA Regulations") that apply when a pension plan has a solvency deficiency. The amount that can be transferred is determined by multiplying the commuted value by the lesser of the most recently determined transfer ratio (essentially solvency assets relative to solvency liabilities, with adjustments) and one. If the plan's transfer ratio is less than one, a plan administrator may only transfer 100% of the commuted value if a remittance is made to the plan equal to the transfer deficiency (the difference between the full commuted value and the amount that can be transferred), or the deficiency is small enough to qualify for the small amount exception. If less than 100% of the commuted value is transferred, the balance is to be transferred by the plan administrator within 5 years after the date of the initial transfer. It is important to note that even if the transfer ratio is one or greater, if the plan administrator "knows or ought to know" that since the most recent valuation report events have taken place that may result in the reduction of the transfer ratio to a value of less than .9, then the plan administrator is prohibited from transferring the full amount of the commuted value without the prior approval of the Superintendent. It is also important to note that a breach of these transfer restrictions is not only a breach of the PBA Regulations but also of the plan administrator's fiduciary obligations. In most Ontario private pension plans the plan administrator is the employer. These transfer restrictions do not apply to transfers made pursuant to reciprocal transfer agreements. If you have any questions regarding these transfer restrictions, please contact a member of the Toronto Pensions and Benefits Group.

PLAN BENEFICIARIES SUCCESSFUL IN FORCING DISCLOSURE OF LEGAL OPINION OBTAINED BY TRUSTEES

In a recent British Columbia decision, beneficiaries of a pension plan were granted access to a legal opinion that was prepared for the trustees who administer the plan (the "Trustees"). In the case *Camosun College Faculty Association, et al* v. *College Pension Board* (decision dated July 14, 2004), the legal opinion obtained by the Trustees (which had presumably been paid for by the pension fund), was made available to the plan beneficiaries on the basis that the Trustees and the beneficiaries had no competing interests, but rather a common interest in the proper administration of the trust. The Court concluded that based on the facts of this case, there was no legal privilege between the Trustees and the plan beneficiaries. The Court might have come to a different conclusion if it had been an employer that had been the plan administrator, who had obtained the opinion in that capacity.

The outcome of this case is similar to other Court decisions (e.g. *Froese, Hockin*) in which legal opinions and actuarial reports that had been paid for by the pension fund had to be produced for the plan beneficiaries.

If you would like more information about this case, please contact a member of the Toronto Pensions and Benefits Group.

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This newsletter is designed to supply brief details of recent legislative or other initiatives of interest and some commentary. The summaries and comments provided are, of necessity, brief and should not be relied upon as legal advice. We encourage you to contact any of the lawyers listed above for further details or advice in the context of a particular situation.