
Amendments to the Federal Pension Legislation

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LEGISLATION

Amendments to the Federal Pension Legislation

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The 2010 Federal Budget bill, entitled the *Jobs and Economic Growth Act*,¹ received Royal Assent on July 12, 2010. Important for plan sponsors of federally regulated pension plans, the budget legislation contains a variety of amendments to the federal *Pension Benefits Standards Act, 1985* (the "PBSA"). This article serves to outline some of these key PBSA amendments.

This article will also review changes to the *Pension Benefits Standards Regulations, 1985* (the "PBSR"), which came into effect on July 1, 2010. These changes include amendments to the investment rules that will impact both sponsors of federally regulated pension plans, and sponsors of provincially regulated pension plans in provinces where the federal investment rules are incorporated into provincial pension legislation.

All section numbers in this article refer to the applicable section of the PBSA or PBSR, as the case may be, that has been amended. Amendments to the PBSA come into force either on Royal Assent, or on a day or days to be fixed by order of the Governor in Council (this date has not yet been fixed, and so the effective date of some amendments are not yet known).

Member Benefits

A number of the PBSA changes serve to enhance the minimum standards applicable to member benefits.

Immediate Vesting

Whereas the PBSA currently permits up to a two-year vesting period for new plan members, the amendments provide that a member will be immediately vested in benefits

on plan enrolment (section 17). The amendment applies retroactively, so, upon the effective date, all pension plan members will be immediately vested in their entire benefit. Many plan sponsors will be required to amend their plans once the new vesting rule comes into force, although some may also wish to consider implementing or extending the waiting period imposed before an employee is eligible to become a plan member (the PBSA permits a waiting period of up to two years for full-time employees, and at least two years and certain earnings or hours of work thresholds for other than full-time employees).

Simplified Pre-retirement Survivor Benefits

The payment of pre-retirement survivor benefits (section 23) has been simplified. Distinctions in respect of whether or not a member was eligible for retirement, has an eligible spouse, or accrued the benefit pre-1987 or post-1986, have been removed. These amendments also provide that a survivor benefit is now payable to a designated beneficiary if there is no surviving spouse, or, if there is no beneficiary, to the estate of the member or former member.

Cost Sharing Rule

The 50% cost sharing rule for contributory defined benefits (member contributions cannot pay for more than 50% of the value of the accrued benefit) has also been simplified in the sense that it applies in respect of benefits accrued for all years of service (section 21).

Marriage Breakdown

There are a few new rules regarding pension credit splitting on marriage breakdown. If a member has had a marriage breakdown agreement or court order which provides that no part of his or her benefit must be divided and paid to the former spouse, the pension plan may provide that the member's pension be paid in the normal form rather than as a joint and survivor pension (section 25).

Variable Benefits

Finally, the amendments allow defined contribution pension plans to provide variable benefits to members eligible for an immediate pension benefit, as long as the pension plan has not been wholly terminated and the

¹ S.C. 2010, c. 12.

member's spouse or common law partner consents (sections 16.2 to 16.4). Variable benefits are similar to registered retirement income fund benefits in the sense that, subject to the parameters of the Income Tax Act,² retirees have more flexibility to determine the amount of income withdrawn annually and how the funds are invested. The amendments also specify that a former member, or his or her survivor, have the right at least once each year to elect to transfer the remaining pension amount to another pension plan or prescribed retirement savings plan, or to use it to purchase a prescribed, immediate or deferred life annuity.

Funding and Security of Benefits

A number of the PBSA changes are in respect of plan funding and/or improving the security of benefits for pension plan members.

Funding Obligations on Plan Termination

The PBSA changes require that pension plan sponsors fully fund pension deficits on full plan termination, setting out a more comprehensive list of the sponsor's funding obligations (section 29). Precise funding amounts and timing are to be prescribed in the PBSR. However, upon full termination of the plan, or the liquidation, assignment or bankruptcy of the employer, the amount required to fully fund pension benefits as at the date of termination is payable immediately.

Letters of Credit

The amendments expand the circumstances under which letters of credit can be provided as security to the plan trustee in lieu of making special payments for solvency deficiencies, making them a permanent tool as long as circumstances are in compliance with the legislation (sections 9.11 to 9.15). The amendments provide specifically that costs associated with obtaining, holding, amending or cancelling a letter of credit may not be paid out of the pension fund.

Deemed Trust Provisions

The existing deemed trust provisions of the PBSA provide that certain sums are held in trust by the plan sponsor for the benefit of plan beneficiaries, thus giving the plan

beneficiaries priority over other creditors. The amendments expand the deemed trust provisions to include the amount of the payment required from the employer if a letter of credit has not been honoured by the issuer, amounts that are due under a workout agreement for plans in distress, and payments required to amortize a solvency deficiency to the extent that such payments have come due and have not been paid (section 8).

Solvency

The Superintendent's consent is now required for the purchase of an annuity if the purchase would impair the pension plan solvency (section 26.1). The Superintendent's consent is also required to authorize a pension plan amendment that will reduce the solvency ratio of the plan to below a prescribed level, or that will increase pension benefits or pension benefit credits where the solvency ratio of the plan is already below a prescribed level (section 10.1). Without such consent, these amendments will be considered void. In addition, the amendments provide that solvency payments may be reduced for a Crown corporation employer if certain prescribed conditions have been met, although such reduction does not apply in respect of amounts deducted from member's remuneration (section 9.16).

Reducing Pension Benefits

The amendments specify that a multi-employer pension plan may be amended so as to reduce pension benefits or credits, even if the plan text does not permit it (section 10.11). However, such amendments will still require the Superintendent's consent.

Distressed Plan Workout Scheme

The amendments add a new distressed plan workout scheme to the PBSA. These changes are aimed at defined benefit plan sponsors who anticipate that they will not be able to make required solvency payments or who are subject to proceedings under the *Companies' Creditors Arrangement Act* ("CCAA") or Part 3 of the *Bankruptcy and Insolvency Act* ("BIA") (sections 29.01 to 29.3). These provisions allow the sponsor to enter into negotiations with a plan member and beneficiary representative in order to conclude a workout agreement that sets out an alternative funding schedule for the plan.

²R.S.C. 1985, c. 1 (5th Supplement), as amended.

PENSION PLANNING

If a plan sponsor elects to proceed with negotiations, it must fulfill a variety of requirements and submit prescribed information to the Superintendent and Minister, including completing a declaration with information regarding the sponsor's inability to pay. Any pension contributions that become due during the negotiation period are deferred to the extent specified in the declaration, except for contributions in respect of normal costs and payment of amounts that the employer has already deducted from member remuneration. These deferred contributions plus interest may become immediately due in a number of circumstances, such as if the pension plan is terminated during the negotiation period or there is no workout agreement arrived at by the end of the negotiation period.

Normally, the Superintendent cannot revoke the plan's registration or declare the whole of the plan terminated during the negotiation period. The proposed funding schedule arising from the negotiation must be submitted to the Minister and will only be approved if less than one-third of the members and less than one-third of the beneficiaries object to the scheme within the prescribed period. The cost of applying to court to appoint member and beneficiary representatives, and the reasonable fees and expenses of the representatives must be paid by the sponsor and not out of the pension fund.

The distressed plan workout scheme provisions do not apply if the sponsor is in the process of being liquidated, has made an assignment or has become bankrupt, or the whole of the pension plan has become terminated. Similarly, the scheme does not apply to multi-employer plans or Crown corporations.

Other Amendments

The amendments to the PBSA also address the following areas.

Superintendent's Powers

The amendments enhance the powers of the Superintendent in a variety of ways. First, the Superintendent is now empowered at any time (rather than just only in certain circumstances upon plan termination) to remove a plan administrator and appoint a replacement administrator if the administrator is insolvent or unable to act or if the Superintendent is of the opinion that it is in the best interests of

those entitled to receive benefits under the plan (section 7.6). Second, the Superintendent may designate an actuary to prepare an actuarial report or termination report and to provide the administrator with the report within a specified period, again, if the Superintendent is of the opinion that it is in the best interests of those entitled to receive benefits under the plan (section 9.01). The administrator will be entitled to provide comments on the draft report, but once finalized, the pension plan will have to be funded in accordance with the final report. The amendments also provide that the Superintendent can now declare a pension plan terminated if crediting of benefits to members ceases (section 29).

Partial Plan Terminations

While the Superintendent is still entitled to declare a pension plan partially terminated, a plan sponsor may no longer do so (section 29).

Multi-employer Plans

Certain of the PBSA amendments help to clarify aspects of multi-employer pension plans. The definition of a multi-employer plan has been amended to specify that contributions to the plan may be determined by agreement with the participating employers, collective agreement, statute or regulation, and to clarify that the contributions payable into the plan by each participating employer are those required under such agreement, collective agreement, statute or regulation (section 9). As noted earlier, the amendments provide that a multi-employer pension plan cannot proceed under the distressed pension workout scheme (section 29.01) and that an amendment to a multi-employer plan that reduces pension benefits or credits is acceptable even if the plan text does not permit it, although the Superintendent's consent for such amendment is required (section 10.11).

Information

The amendments expand requirements for providing information to former members. Annual statements now have to be supplied to former members and their spouses or common law partners (section 28). Anyone entitled to benefits under a plan, and their spouses or common law partners, will be entitled to examine and request copies of further documents, such as reports prepared by

a designated actuary on request of the Superintendent, letters of credit used to fund solvency deficiencies and certain information respecting the formation of a distressed pension workout scheme. The PBSA also now requires that where a plan is terminated, the administrator provide a written statement regarding the termination, as well as information in respect of individual benefits, to each member and former member, and their spouses or common law partners. This obligation must be described within the pension plan text.

Regulation-making Power

The changes give the Governor in Council a variety of additional regulation-making power. Such authority extends to letters of credit, the distressed pension plan scheme, variable benefits and the meaning of "impair the solvency" for the purpose of transferring monies out of a pension fund or purchasing a life annuity, among other matters (section 39).

Increase in Pension Surplus Threshold (Income Tax Act)

The *Jobs and Economic Growth Act* also provides for an amendment to the Income Tax Act that will increase the pension surplus threshold from 110% to 125% for post-2009 contributions regarding post-2009 periods of pensionable service. This means that a larger surplus cushion can be built up to protect against market downturns or other types of difficult financial circumstances. The increase in the pension surplus threshold applies to all pension plans, both federally and provincially regulated. However, the employer's ability to access any such surplus will continue to be governed by applicable pension legislation and the terms of the pension plan text.

Changes to the Regulations

New provisions of PBSR have also now come into effect (more are anticipated).

Three-year Average Solvency Ratios

The PBSR now provides for the use of average solvency ratios (rather than the current solvency ratio) to determine minimum funding requirements (section 9). Intended to reduce the effect of short-term fluctuations in

the value of plan assets and liabilities on funding requirements, the solvency position of the plan will now be assessed using the average solvency ratio, based on the market value of plan assets over the current and previous two years. Annual filing of valuation reports will be required to put this funding model into effect and past deficiencies will be consolidated annually, but the amortization period remains at five years. There are also a variety of transitional rules that are designed for the period between the current funding rules and the point at which the three-year average model can be fully adopted.

As a result of these amendments, the Office of the Superintendent of Financial Institutions ("OSFI") has released the change to section 2 of the *Directives of the Superintendent*. The change sets out the frequency requirements for the preparation of actuarial reports described in subsection 12(3) of the PBSA, including the requirement for annual valuation in certain circumstances. OSFI has also extended the deadlines for actuarial reports required to be filed for a plan year ending December 31, 2009 to February 28, 2010. These will now be due by September 15, 2010.

Contributions and Contribution Holidays

Required contributions will have to be remitted on a monthly basis as of January 1, 2011 (section 9). In addition, contribution holidays will only be permitted if a plan's solvency ratio exceeds full funding plus a solvency margin set at 5% of solvency liabilities. This is intended to create a funding cushion in order to protect plan benefits.

Investment Limits

The new regulations remove the 5, 15 and 25% quantitative investment limits regarding resource and real property investments from section 10 of Schedule III to the PBSA. This change is relevant to pension plan sponsors of both provincially and federally regulated plans as Schedule III is generally incorporated into provincial pension legislation. Further revisions to the Schedule III investment rules are anticipated.



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