FTR Now

Implementing Phase One of Ontario Pension Reform: A Roadmap for Plan Sponsors and Administrators

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On Tuesday, May 18, 2010, Bill 236, the *Pension Benefits Amendment Act, 2010* ("Bill 236"), the first major piece of pension reform legislation to be approved by the Ontario Legislature in over two decades, received Royal Assent. The Bill 236 amendments enhance certain individual member rights and entitlements, provide the Superintendent of Financial Services with expanded oversight powers and include new wind-up and asset transfer rules. Sponsors and administrators of Ontario-registered pension plans and plans having Ontario members need to take steps to change plan texts and administration practices, and also consider the implications of this important legislation from an employment law and labour relations perspective. In this *FTR Now*, we provide a high-level roadmap to help you to identify necessary or desirable changes, with a primary focus on single employer pension plans.

BACKGROUND

As reported in our December 15, 2009 *FTR Now*, Bill 236 was introduced on December 9, 2009, marking the beginning of the Ontario government's multi-stage pension reform process. While certain Bill 236 amendments to the Ontario *Pension Benefits Act* ("PBA") are now in force, others will not take effect until a date to be named by proclamation of the Lieutenant Governor. That date has not yet been announced. In addition, some of the new statutory rules will require supporting regulations before they can be fully implemented.

For a full review of the changes to the PBA resulting from Bill 236 as it was first introduced, click here to see our December 15, 2009 *FTR Now*.

PLAN AMENDMENTS

Virtually all pension plans having members in Ontario will need to be amended as a result of Bill 236. Defined benefit ("DB"), defined contribution ("DC") and hybrid plans are all affected. The extent to which your plan will need to be amended will, of course, depend upon its existing terms. We expect that most plans will need to be amended to reflect at least some of the changes outlined below.

IMMEDIATE VESTING AND LOCKING-IN

Both DB and DC plans will be required to provide immediate vesting and locking-in of pension benefits to members who terminate on or after the date this rule is proclaimed in force. Prior to Bill 236, the PBA required vesting and locking-in after two years of plan membership. As a result, many plans will need to be amended to comply with the new requirements.

Plan sponsors might wish to examine the eligibility provisions of their plans in light of the move to immediate vesting. Increasing the waiting period may minimize the costs associated with enrolling and terminating short service employees. The maximum waiting period for full-time employees continues to be 24 months of continuous employment. You will need to consider whether there are any restrictions on your ability to lengthen the waiting period under your plan (e.g., due to the terms of a collective agreement).

SMALL BENEFIT COMMUTATION AND UNLOCKING

Immediate vesting and locking-in may lead to a larger number of members terminating with short service and small benefit entitlements. Bill 236 eases the burden associated with administering these small benefits by relaxing the threshold for small benefit unlocking. The current threshold permits a plan to commute and pay in cash the value of the pension benefits of a former member if the annual pension payable at the former member's normal retirement date is 2% or less of the Year's Maximum Pensionable Earnings ("YMPE") in the year of termination of employment. Bill 236 increases this threshold to 4% of the YMPE. Bill 236 also amends the PBA to allow for unlocking if the commuted value of the former member's pension is less than 20% of the YMPE in the year of termination of employment. In addition, the small benefit rule is extended to apply to survivor benefits. The new small benefit commutation limits will not be effective until they are proclaimed to be in force.

Although DB and DC plans are not required to reflect this rule, most plans contain the existing rule and most employers will wish to take advantage of the higher threshold in order to reduce the costs of administering small pensions.

ENTITLEMENT TO GROW-IN BENEFITS ON TERMINATION

Many single employer DB plans will require some form of amendment to reflect the fact that "grow-in benefits" will be extended to most members with 55 age plus service points whose employment is involuntarily terminated. This entitlement, which takes effect on July 1, 2012, is discussed in greater detail below. Jointly-sponsored and multi-employer pension plans can opt out of providing these benefits to their members.

OTHER PROVISIONS

There are a number of other Bill 236 changes that on a case-by-case basis could necessitate plan amendments. For example, changes to member notice requirements, elimination of partial plan wind-ups (which will take effect in 2012), and new Pension Advisory Committee rules could necessitate plan amendments. Employers will need to review their plans to determine whether amendments to reflect these changes are necessary or desirable.

In addition, Bill 236 permits phased retirement pensions for Ontario members of DB plans. Phased retirement is not a mandatory plan provision. A DB plan may be amended to offer phased retirement to members who satisfy the conditions on the terms set out in the legislation. Some implications of phased retirement from a workforce management perspective are discussed further below.

PLAN ADMINISTRATION CONSIDERATIONS

Plan administrators will also need to adjust their administration practices in the following areas.

SYSTEMS

Computer systems which support day-to-day plan administration will need to be updated. For example, if an employer wishes to implement phased retirement, this may require significant changes to pension administration software to support the necessary phased retirement elections and calculations.

COMMUNICATIONS

NOTICE OF PLAN AMENDMENTS

Bill 236 changes three key aspects of plan amendment notices: who will receive notice, what the notice must contain, and when it must be provided. First, the “who”. Currently, plan administrators need only provide notice of a plan amendment to members, former members and other persons affected by the amendment. Bill 236 requires that all members, former members and retired members receive notice of all plan amendments, irrespective of whether they are “affected” by the amendment. Notice must continue to be provided to any trade union that represents plan members.

The content of plan amendment notices may also change. Currently, the PBA simply states that a plan administrator must provide a “notice containing an explanation of the amendment”. Bill 236 contemplates the issuance of regulations that will prescribe what a plan amendment notice must contain. At a minimum, such regulations will likely include such basic data as the name and registration number of the plan, but the regulations may also require specific information to be included in the explanation of the amendment, such as when the amendment is effective and who is affected by it.

Finally, Bill 236 may change when notice of amendments must be provided. Currently, it is common practice for plan administrators to file certain amendments with the Financial Services

Commission of Ontario (“FSCO”) and to provide notice of the amendment after the amendment is filed, often in the next annual pension statement issued to members. Under the new regime, advance notice will have to be provided before an amendment is filed unless the amendment fits within an exception prescribed by regulation. Those regulations are pending.

As a result of these changes, plan sponsors will have to rethink when and how they approve, announce and implement future plan amendments, including any amendments that may result from the enactment of Bill 236.

BENEFIT OPTION STATEMENTS AND EMPLOYEE BOOKLETS

Plan administrators must ensure that benefit option statements provided to terminated and retired members as well as employee booklets are updated to reflect the various changes introduced by Bill 236, such as immediate vesting and locking-in. Forms may also need to be updated to allow former members and survivors the option to transfer non-locked-in amounts (such as small benefits, excess contributions and pre-retirement death benefits) directly to an RRSP or RRIF in their name.

In addition to updating forms, it is also an opportune time to revisit pension administration procedures and processes relating to employee terminations to ensure small benefit entitlements get transferred out of a plan rather than remain in the plan as deferred pensions.

ELECTRONIC COMMUNICATIONS

Bill 236 amends the PBA to confirm plan administrators’ ability to communicate electronically with plan members who consent. Electronic communication most often consists of delivery of notices and documents by e-mail and the maintenance of a corporate intranet or secure internet website from which members can access plan information, reports and other documents. Since universal consent to electronic communication is virtually impossible to obtain, in most cases electronic delivery of pension information will have to operate in parallel with paper-based communications (rather than replace paper communications altogether). However, in some workplaces – such as office environments where most pension plan members have access to a computer terminal and company e-mail – there may be sufficient member uptake to make electronic communication of pension information worthwhile.

Since notice of plan amendments will have to be provided to a broader group of people, the time may be right for some plan administrators to consider introducing electronic pension communications or expanding their efforts to obtain universal consent in this regard. In that case, administrators should plan ahead, since the process of advising members of their rights with respect to electronic pension communication and obtaining their consent can take some time.

RECORDS RETENTION

Given the long-term nature of pension entitlements, it is generally good practice to retain pension records indefinitely. Bill 236 introduced statutory records retention requirements to the PBA. Once supporting regulations are issued, plan administrators will need to ensure that, from a statutory compliance perspective, prescribed records are retained for the prescribed period of time. It is also anticipated that FSCO will be issuing a new records retention policy to complement the new regulations.

In many cases, plan administration functions are outsourced to third parties. In such cases plan administrators should start a dialogue with all third party service providers to ensure that records retention issues are adequately addressed in the relationship. Plan administrators should also ensure that all contracts with third party service providers reflect the agreed upon arrangement.

WORKFORCE MANAGEMENT CONSIDERATIONS

Certain aspects of Bill 236 will have real implications for your organization from a workforce management perspective. In turn, these implications may affect coming rounds of collective bargaining as well as individual employment arrangements.

GROW-IN BENEFITS

Currently “grow-in benefits” are additional benefits provided to certain plan members when a plan is wound up, in full or in part. Grow-in benefits are currently required to be taken into account in an employer’s solvency funding obligations. Under Bill 236, effective July 1, 2012, grow-in benefits will extend to all involuntary “without cause” terminations for plan members who have 55 age plus service points. This change will affect the employer’s “normal costs” funding obligations because it will increase the benefits paid from a plan in situations other than plan wind-ups.

As a result, some employers may wish to reduce or eliminate early retirement subsidies and bridge benefits under their plan before the relevant provisions of Bill 236 take effect on July 1, 2012. However, before reducing early retirement subsidies, employers will have to consider a number of factors including the potential impact of scaling back early retirement subsidies on workforce management. For example, altering early retirement subsidies may not be appropriate where an employer wishes to incent employees to retire prior to normal retirement age.

In a unionized setting, depending on the language of your collective agreement, the reduction of early retirement subsidies may need to be collectively bargained to the extent that these incentives apply to members of a bargaining unit. Even if the reduction of early retirement subsidies is not achievable, it will be important to understand the cost implications of expanded grow-in benefits under Bill 236 so that you can ensure these costs are considered when negotiating other wage and benefit demands.

To the extent that early retirement subsidies are not eliminated from a plan, all human resources staff will need to understand the new pension implications of characterizing a separation of employment in one way or another. For example, currently it generally does not matter from a pension perspective whether a separation of employment is characterized as a “without cause” termination or a resignation. Starting July 1, 2012 an employee will be entitled to grow-in benefits in the former case but not the latter, and this difference will have implications for offers made to departing employees.

PHASED RETIREMENT

Phased retirement will, to the extent permitted under the *Income Tax Act* (Canada), become available in Ontario when the relevant provisions of Bill 236 are proclaimed in force. Phased retirement can be a tool to assist employers retain experienced, long-service employees who might otherwise wish to retire. Phased retirement can achieve this by allowing the employer and employee to enter into an arrangement under which the employee commences to receive a partial pension while continuing to work (typically on a reduced hours basis). Such arrangements can be particularly helpful where it may take a significant amount of time to train a replacement for the employee who is transitioning into retirement. However, phased retirement can have unintended consequences if essential employees choose to reduce their working hours and the employer cannot replace the lost capacity.

For employers who wish to add phased retirement pensions or who have already added those provisions in respect of members in other provinces where phased retirement was already permitted, plan amendments will be necessary. Employers considering phased retirement will need to take into account its potential impact on employee and labour relations and production requirements. For example, if phased retirement is made available, human rights concerns will likely constrain the employer’s ability to “cherry-pick” the employees to whom a phased retirement arrangement will be offered. Consequently, employers who implement phased retirement will most likely have to make it available to employees based on *bona fide* workforce requirements and objective criteria. With a unionized workforce, the union will undoubtedly wish to negotiate the terms and conditions under which phased retirement will be made available.

For these and other reasons, employers who may have a legitimate need to offer phased retirement should start considering whether they wish to offer phased retirement, and the policies necessary to ensure that phased retirement can be successfully integrated into their workplace.

GOVERNANCE CONSIDERATIONS

The purpose of a pension advisory committee (“PAC”) is to monitor a pension plan’s administration, to make recommendations with respect to the plan’s administration and to increase members’ understanding of their plan. Relatively few PACs have been established to date. However, Bill 236 makes it easier for members to establish and operate a PAC. Plan administrators need to be prepared to meet their new legal obligations to assist in the establishment and operation of a PAC.

IMPLICATIONS FOR NON-RPP ARRANGEMENTS

The amendments required by Bill 236 may also affect other workplace benefits such as supplementary pension arrangements or savings plans, which “rely on” the terms of a registered pension plan (“RPP”). For example, if vesting under a supplementary pension plan is tied to vesting under a base RPP, the employer should consider whether this is still appropriate once RPP benefits vest immediately. We encourage you to review your supplementary plans and other benefit plans which are related to your RPP to determine whether any changes to these corollary plans are necessary or desirable in light of Bill 236.

TYING UP LOOSE ENDS

ASSET TRANSFERS RESPECTING PAST SALES OF BUSINESSES

For some time, regulatory policy has effectively placed a moratorium on most asset transfers between DB pension plans. Prior to the moratorium, such transfers had been a means of consolidating pension benefits in a purchaser’s pension plan when employees transferred between companies in the context of a sale of business. As noted in our December 15, 2009 *FTR Now* , Bill 236 will open up a window within which pension plans affected by a past restructuring may enter into an asset transfer agreement to facilitate such consolidation. That window will be open until July 1, 2015, and employers who were previously barred from making an asset transfer in conjunction with a past corporate transaction or business reorganization may wish to explore making an asset transfer in appropriate cases.

For those of you who are in the midst of negotiating a corporate transaction or have a deal on the horizon, you will need to consider the new Bill 236 asset transfer regime, although the new regime will not be effective until a date to be named by proclamation of the Lieutenant Governor.

PARTIAL PLAN WIND-UPS

While partial wind-ups are often thought of as something to be avoided, they can also be a helpful tool where an employer is looking to settle benefits in respect of a group of employees whose benefits are “frozen” in a particular plan. Since partial wind-ups will no longer be available effective January 1, 2012, employers for whom a partial wind-up may be desirable should start considering whether and how they wish to take advantage of Ontario’s partial wind-up regime before it is no longer available.

NEXT STEPS

Now that parts of Bill 236 have come into force, sponsors and administrators of Ontario-registered pension plans and pension plans with Ontario members should carefully assess the implications of this significant piece of legislation for their businesses and pension plans.

In virtually all cases, Bill 236 requires significant changes to a pension plan text, an organization's pension administration practices and its pension governance processes. Bill 236 presents challenges as well as opportunities from a workforce management perspective. In all cases, the impact Bill 236 will have on your organization and your pension plans will depend on the existing terms of your pension plan and your workforce characteristics.

The Ontario government has announced that further legislative reform will be forthcoming. We will keep you apprised of further developments.

To discuss further how Bill 236 affects your business and your pension plan, please contact any member of the Pension & Benefits Group or your regular Hicks Morley lawyer.