FTR Now

Ontario Introduces Bill 120, the Securing Pension Benefits Now and for the Future Act, 2010

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As reported in our previous *FTR Now*, on October 20, 2010 the Ontario government introduced Bill 120, the *Securing Pension Benefits Now and for the Future Act, 2010*, reflecting a number of the reforms announced in the government's news release of August 24, 2010. The Bill supplements the first phase of Ontario pension reforms, contained in Bill 236, the *Pension Benefits Amendment Act, 2009*, which was passed earlier this year. Bill 120 is a further, significant step in the overhaul of Ontario's pension legislation, the *Pension Benefits Act* ("*PBA*") — the first in over two decades.

The reforms contained in Bill 120 encompass a range of significant pension issues, including changes to the types of permissible benefits and pension plans, as well as changes to surplus entitlement and withdrawal rules, plan administration matters, regulatory oversight, and Pension Benefits Guarantee Fund ("PBGF") coverage.

This *FTR Now* reviews the key aspects and potential implications of Bill 120.

EXPANDING THE FRAMEWORK FOR BENEFIT TYPES

The *PBA* has generally contemplated two types of pension benefits – defined benefits ("DB") and defined contributions ("DC"). Bill 120 contains several provisions that would, if passed, both clarify and expand on the types of benefits that could be made available under Ontario registered pension plans.

DEFINED BENEFITS

The definition of "defined benefit" is to be amended to mean pension benefits other than DC benefits or target benefits. As explained in more detail below, this may include optional benefits.

OPTIONAL BENEFITS

Bill 120 proposes new "optional benefits", which would enable Ontario registered DB pension plans to provide flexible pensions, as permitted under the *Income Tax Act* ("*ITA*"). The Bill provides for optional benefits to be purchased by way of optional contributions, which must be made entirely by plan members. No employer contributions may be used to obtain optional benefits.

Bill 120 proposes to exempt optional benefits from certain *PBA* minimum requirements (e.g. the 50% rule). Other rules governing optional contributions and the conversion of optional contributions to optional benefits are to be prescribed.

If Bill 120 is passed, optional benefits will provide employers with a plan design alternative that could assist with the delivery of enhanced retirement benefits, but without a corresponding additional funding obligation on the part of employers.

TARGET BENEFITS

Bill 120 introduces "target benefits", as a new type of pension benefit. Key features of target benefits are that the contributions are fixed by collective agreement, benefits can be reduced at the discretion of the plan administrator, and special payments are not required in respect of solvency deficiencies.

Most of these features are in fact set out as qualifying criteria. Specifically, pension benefits will be considered target benefits if all of the following are satisfied:

> (a) the pension benefits are not DC benefits;
> (b) the employer's obligation to contribute to the pension plan is limited to a fixed amount set out in one or more collective agreements; and
> (c) the administrator's authority to reduce benefits, deferred pensions and pensions is not restricted (by the pension plan and fund documents, by collective agreement, or by applicable pension legislation) either while the pension plan is ongoing or upon wind up.

In theory, benefits under existing multi-employer pension plans ("MEPPs") might already satisfy the above requirements and, with the passage of Bill 120, become plans that provide for target benefits. However, plan documentation and/or collective agreements will in many cases impose limitations or parameters on the ability of an administrator to unilaterally reduce benefits, and in these situations it will be necessary to make changes to documentation or agreements in order for MEPP benefits to qualify as target benefits, even if only on a limited basis (i.e., for future service).

Target benefits might also be provided under single employer pension plans (or components of plans) that are established (or added) at a future date, or on conversion of an existing plan, for future service. This is enabled by way of a proposed amendment to section 14 of the *PBA*, the provision that voids amendments which purport to reduce accrued benefits. Bill 120 proposes to amend section 14 to provide that the void amendment rule does not apply in respect of a pension plan that provides only target benefits, or in respect of the part of a plan that provides target benefits. [1]

Bill 120 extends target benefits to multi-jurisdictional plan situations (in circumstances to be prescribed), despite restrictions that may apply under the legislation of other applicable Canadian pension jurisdictions. Further rules regarding the provision of target benefits by multi-jurisdictional plans will likely be required, whether by way of regulations or guidelines or agreements that may be established by the Canadian Association of Pension Supervisory Authorities, which has developed the new multi-lateral agreement amongst designated jurisdictions.

DEFINED CONTRIBUTION PENSION PAYMENTS

A new section would govern the payment of pensions and pension benefits, made in accordance with the *ITA*, from DC plans. The change would allow DC plans in Ontario to provide for pensions to be paid directly from the plan. This form of payment could be offered by a plan as an option, rather than force the transfer of DC assets for the purchase of an annuity or to a locked-in account. Regulations might provide additional guidance regarding the payment of DC pensions and pension benefits.

Similar DC pension payment options are already authorized by the pension standards legislation of a number of other Canadian jurisdictions.

MATTERS AFFECTING PLAN FUNDING

LETTERS OF CREDIT

As expected, the Bill includes provisions to allow prescribed employers to use a letter of credit (LOC) to fund up to 15% of a plan's solvency liabilities. [2] The LOC would be used to reduce or eliminate the special payments that would otherwise be required to fund a solvency deficiency.

The Bill states that the costs of obtaining and maintaining the LOC cannot be paid from the pension fund. On the other hand, the costs of enforcing the LOC can be paid from the fund unless limited by language in the plan that restricts payment of administration fees and expenses out of plan assets. Regardless of a plan's expenses wording, if the administrator is one appointed by the Superintendent, or the Superintendent has assumed responsibility for administering the plan, then the costs of enforcing the LOC can be paid from the fund.

Details concerning the time limits for notifying the Superintendent of the use of the LOC and the circumstances under which the administrator can demand payment under the LOC will be contained in regulations, to be released. [3]

CONTRIBUTION HOLIDAYS

Under Bill 120, contribution holidays for either or both employers and members would be explicitly permitted under the *PBA*, as long as contribution holidays are not prohibited by the pension plan documents, and only if the plan has a "surplus" and prescribed conditions are met. One of the expected conditions (based on the government's pension reform announcement made on August 24, 2010) is a minimum transfer ratio of 105%.

The explicit requirement that the documents not prohibit the holiday suggests that it will continue to be necessary to conduct a full historical review of documentation (i.e., plan texts, funding agreements and employee communications) to determine if a contribution holiday is prohibited under the terms of the plan.

Bill 120 would amend the *PBA* to provide that a reduction or cessation of contributions due to a contribution holiday does not trigger a wind up or partial wind up.

The government's August announcement also indicated that the plan administrator will be required to disclose the contribution holiday to plan members, former members and survivors, and to file annual statements with the Financial Services Commission of Ontario to confirm eligibility. These additional conditions are expected to be included in future amendments to the regulations.

RESTRICTIONS AFFECTING BENEFIT IMPROVEMENTS

As expected, Bill 120 introduces new restrictions on benefit improvements when a plan is underfunded. Amendments that improve benefits will be considered void if the enhancement reduces the plan's transfer ratio or the going concern funded ratio below the prescribed level, which will be specified when the regulations are amended.

Based on the government's August announcement, it is expected that if the transfer ratio of the plan falls to less than 85% or the fund would be less than 85% funded on a going concern basis as a result of the improvement, then a lump sum payment would be required to prevent the reduction in the applicable ratio, and any remaining cost would be payable over a shorter period of up to five years. As well, the government indicated that, even if the improvement does not cause the funded status of the plan to fall below these thresholds, the amortization period for funding improvements on a going concern basis will be reduced to eight years from the current 15.

JSPPS AND SOLVENCY FUNDING

The Bill would amend the *PBA* such that plans which were jointly sponsored pension plans ("JSPPs") on August 24, 2010 will be exempt from the requirement to make contributions to fund a solvency deficiency. The regulations prescribing the funding requirements for JSPPs will need to be amended to fully implement this change. Also, a qualifying JSPP may need to

be amended to reflect that neither the members nor the employers must make solvency contributions.

The above change will potentially benefit existing JSPPs, like OMERS, but will be of little benefit to private-sector employers who may have been considering a move to a JSPP model in the future, unless further legislative relief is provided in respect of other types of plans.

TERMS RESPECTING FUNDING ON EMPLOYER WITHDRAWAL FROM MEPPS AND JSPPS

Bill 120 also proposes amendments that would require MEPPs and JSPPs to specify what happens when a participating employer withdraws from the plan. These plans will need to be amended if they do not already describe the funding and payment of pension benefits for members, former members and survivors affected by the withdrawal.

The Bill notes that prescribed requirements must be satisfied. It is not known at this time what those prescribed requirements will be, or if there will be any, but it is expected that the plan administrator could be required to file with the Superintendent a special report on the plan's viability if a certain percentage of participating employers leave. It is not yet known whether the regulations will specify whether a withdrawing employer is required to fully fund any deficiency associated with its portion of the plan.

ENTITLEMENT TO SURPLUS

Bill 120 proposes to further modify the rules concerning surplus entitlement and withdrawal both on plan wind up (in whole or in part) and for continuing plans.

ON FULL OR PARTIAL WIND UP

Bill 120 provides for surplus arising on a full or partial wind up to be allocated either by an agreement or by way of an arbitration award. [4]

Bill 120 authorizes the Superintendent to consent to the payment of wind up surplus to an employer on the basis of a written agreement, without regard to the ownership of surplus in the current and historical pension plan documentation. Specifically, Bill 120 would facilitate surplus withdrawals based on the agreement of the employer and union, or the employer and two-thirds of the members (where there is no trade union that represents the members) provided that an appropriate number (as determined by the Superintendent) of former members and other persons entitled to pension payments also agree. These "withdrawal on agreement" rules apply to plans that are wound up in full and in part.

If the allocation of pension surplus is not addressed within a set period of time following the full or partial wind up of a pension plan, Bill 120 gives the Superintendent the authority to determine whether an arbitrator ought to be appointed to resolve the dispute.

The employer, plan members, former members, retired members, other beneficiaries, or the applicable unions may propose arbitration as a means of resolving surplus issues. An arbitrator can be appointed by the Superintendent at his own discretion, or by agreement of the parties (identified above) who are otherwise authorized to consent to a surplus withdrawal arrangement. Either way the appointment of an arbitrator commences the arbitration process, and the above parties are deemed to agree to and be bound by the process and any award, which award prevails over historical and current plan and trust documentation. The Superintendent is not a party to any such arbitration.

SURPLUS WITHDRAWALS FROM CONTINUING PLANS

Bill 120 also proposes to change the rules that apply for surplus withdrawals for continuing pension plans. Specifically, it would permit surplus to be withdrawn from continuing plans with the agreement of all relevant parties (the employer, and the

union or, if none, two-thirds of the members) and the consent of former and retired members and other persons as determined by the Superintendent. Bill 120 mandates that a minimum “surplus cushion” remain in the pension plan following a surplus withdrawal.

For most pension plans (being those where all pension benefits are not guaranteed by an insurance company) the retained surplus must equal the greater of the following amounts:

(a)the sum of (i) two times the normal cost of the plan, and (ii) 5% of liabilities; and
(b)25% of plan liabilities

IMPLICATIONS

It is expected that the agreement and arbitration proposals under Bill 120 will, if passed, facilitate surplus withdrawals from both continuing and wound up pension plans.

Where surplus exists in a pension plan that is wound up (in whole or in part), parties will wish to assess both approaches with a view to the possible outcomes, including the likely allocation, potential timing and related costs before deciding on a surplus withdrawal strategy. It is anticipated that the Superintendent will refrain from unilaterally appointing an arbitrator where parties are actively working towards a negotiated solution.

ADMINISTRATION OF PENSION PLANS

A variety of proposed amendments are made with respect to the administration of pension plans.

PAYMENT OF ADMINISTRATIVE FEES AND EXPENSES

A new section governing the payment of fees and expenses would authorize payment of reasonable amounts from the pension fund respecting the administration of a pension plan and the administration and investment of the pension fund. The provision would apply to payments to the administrator, to agents of the administrator, to the employer or to any other person who provides services relating to the administration of the pension plan or the pension fund. [5]

However, such payment would not be authorized if payment is prohibited or payment of the fees and expenses is otherwise provided for, either under the documents that create and support the pension plan or the pension fund, or under the *PBA* or regulations.

Generally, the proposed scheme is the legislative response to the Supreme Court of Canada’s decision in the *Nolan v. Kerry (Canada) Inc.* case. In *Kerry*, the Supreme Court found that the plan/trust documents will be determinative of whether fees and expenses can be paid from the pension fund. Silence in the documents does not imply that the employer must pay plan expenses. Provided nothing in the documents requires the employer to pay expenses, reasonable expenses can be paid from the fund. Moreover, if payment of expenses out of the fund is permitted under the plan documents and the expenses are reasonable, it does not matter whether the services are provided by agents or third parties or by the administrator or employer.

Of interest, the proposed amendments in Bill 120 require only that fees and expenses be “reasonable”, and eliminate the “usual” component under the *PBA* as currently constructed. Also, the proposed amendment expressly covers the fees and expenses for services provided in respect of both the pension fund and the plan.

REIMBURSEMENT OF EMPLOYER

Currently, the *PBA* provides for the reimbursement of an employer for overpayments into a pension fund. Bill 120 proposes to amend these provisions to authorize employer reimbursement from the pension fund where an employer either:

> (a)pays an amount in respect of the pension plan that should have been paid out of the pension fund; or
> (b)makes an overpayment into the pension fund. Reimbursement to the employer from the pension fund is not permitted unless the plan administrator has received the prior consent of the Superintendent.

Also, the timelines are to be extended. Under the current rules, the application for reimbursement must be within the same fiscal year in which the overpayment or payment occurred. The deadline for applying for reimbursement is to be changed to the later of:

> (a)24 months after the date on which the employer made the payment or overpayment; and
> (b)six months after the date on which the administrator, acting reasonably, becomes aware of the payment or overpayment.

The extension of the deadline for applying for a reimbursement will be welcome change for employers.

PUBLIC SECTOR PENSION PLANS, EMPLOYEE TRANSFERS TO THE FEDERAL PUBLIC SERVICE

Bill 120 introduces a new section applicable to Ontario public sector employees who are transferred to the federal public service in connection with the sale of a business to the government of Canada. The change would permit the assets of such employees to be transferred from their current public sector plan to the Public Service Superannuation Plan (Canada), subject to the prior consent of the Superintendent.

THE PENSION BENEFITS GUARANTEE FUND

The proposed amendments in Bill 120 would increase the existing eligibility threshold for PBGF coverage from three to five years. Specifically, pensions and pension benefits would not become eligible for PBGF coverage until a plan has been established or maintained for five years. Similarly, PBGF coverage would not apply to pension or pension benefit increases made effective within the five year period preceding the plan's wind up date.

PBGF coverage will not apply to the new types of pension benefits introduced in Bill 120 – target benefits and optional benefits. Consistent with the current legislation, PBGF coverage will not apply to JSPPs or MEPPs.

REGULATORY OVERSIGHT AND ENFORCEMENT

Prior reforms proposed in Bill 236 enhanced the oversight powers of the Superintendent (see our December 15, 2009 *FTR Now*). Bill 120 further expands these powers.

APPOINTMENT OF AN ADMINISTRATOR

Amendments proposed by Bill 120 would expand the circumstances in which the Superintendent would be authorized to terminate and/or appoint a plan administrator. The Superintendent would also be authorized to act as a pension plan administrator. The conditions governing the Superintendent's authority are to be prescribed by regulation. Presently, the Superintendent is authorized to appoint a plan administrator only in connection with the wind up of a pension plan, and the Superintendent has no authority to act as a plan administrator.

ACTUARIAL METHODS AND ASSUMPTIONS

Bill 120 contains proposed amendments that would grant additional powers to the Superintendent to impose restrictions on the actuarial methods and assumptions used in the preparation of reports on pension plans or pension funds. Specifically, if the Superintendent determines that the methods used to prepare a report are inconsistent with accepted actuarial practice, or inappropriate in the circumstances of the pension plan, the Superintendent could order that the plan administrator prepare a new report. Clearly, this change would give the Superintendent a much broader power to impose actuarial methods and assumptions based on the circumstances of a particular pension plan.

Further, Bill 120 would authorize the making of regulations to prescribe requirements and restrictions applicable to the actuarial methods and assumptions to be used in reports.

When the Superintendent intends to make an order regarding the administration of a pension plan, a notice of the proposed order must be issued. If there is disagreement respecting actuarial methods and assumptions to be used in a report and the Superintendent subsequently issues a notice of proposal to order that actuarial methods and assumptions be changed, employers and plan administrators (as well as other interested parties) will have an opportunity to request a hearing to oppose the Superintendent's proposed order.

PROPOSED DECISIONS

Currently, section 89 of the *PBA* imposes specific requirements on the Superintendent when he or she proposes to refuse to register a pension plan or an amendment to a pension plan or to revoke a registration. Bill 120 would make technical changes to the language used in this section, repealing the sections which refer to the Superintendent's decision as a "proposal" and rewriting them using the term "intended decision" instead.

EXTENSION OF DEADLINES

Currently, the *PBA* authorizes the Superintendent to extend procedural time limits where the Superintendent is of the view that there are reasonable grounds for doing so. Bill 120 would expand these powers, allowing for the extension of substantive deadlines for the filing of documents, as well. The proposed amendments allow for deadlines to be extended to a maximum of 60 days, or further if the Superintendent is satisfied that extraordinary grounds exist, and that no one will be prejudiced by a longer extension. This is a positive change as it will allow for relief from deadlines where an extension is warranted.

OTHER

ONGOING REVIEW OF *PBA* AND REGULATIONS

Another amendment proposed by Bill 120 would require that the Minister of Finance initiate a review of the *PBA* and regulations, or a portion of the *PBA* and regulations, at least every five years. This mandated, regular review of pension legislation should assist with making amendments that respond to changes in the pension landscape, and to resolve issues that may exist in the legislation and that are discovered over time.

CONCLUSION AND NEXT STEPS FOR EMPLOYERS

Bill 120 passed first reading on October 19, 2010, and at the time of writing the second reading of the Bill was in the process of being debated. It is not known when the Bill will become law and it is possible that revisions may be made in the interim. Employers will want to track the passage of the Bill and to review and understand the supporting regulations when they are released. Our Pension & Benefits Group will keep you apprised of these developments.

If you wish to follow the legislative developments respecting Bill 120, please visit or subscribe to our Legislative Blog.

If you have any questions about how Bill 120 may affect your business, or your pension plan, please contact any member of the Pension & Benefits Group.

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[1] Existing subsection 14(3) of the *PBA* already authorizes amendments to reduce defined benefits where the obligation of the employer to contribute is limited to a fixed amount set out in a collective agreement. A key difference between these types of defined benefits and the proposed "target benefits" is that in the latter case the administrator has unfettered discretion to reduce benefits in the case of target benefits.

[2] Public sector pension plans and MEPPs are generally excluded from utilizing LOCs.

[3] A unique solvency liabilities calculation applicable to the 15% limit could be prescribed by regulation.

[4] With the elimination of partial wind ups on the horizon, the surplus provisions relating to partial wind ups are clearly provided only as a transitional measure. Bill 120 provides for these new rules to apply to wind ups (in whole or in part) that are now in progress (i.e., where the wind up date falls before the date that the Bill 120 changes take effect), subject to any requirements that may be prescribed.

[5] This would include the Superintendent, if the Superintendent assumes administrative responsibility, or any administrator appointed by the Superintendent.

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