FTR Now

Ontario Budget – Highlights for Employers

Date: March 29, 2012

On Tuesday, March 27, the Ontario Government introduced its 2012 Budget, which is entitled *Strong Action for Ontario* (the "Budget"). The Government also introduced Bill 55, the *Strong Action for Ontario Act (Budget Measures)*, *2012* ("Bill 55"), omnibus legislation designed to implement a number of the proposals contained in the Budget.

The Budget sets out the Government's plan to reduce a budget deficit that currently stands at over $15 billion, such that Ontario would have a zero deficit by the 2017-18 fiscal year. To that end, the Budget contains a number of significant restraint measures, and seeks to restructure large elements of the broader public sector ("BPS") in an effort to more efficiently deliver public services.

In this *FTR Now*, we will consider the provisions of the Budget, with a special emphasis on those proposals that relate more directly to human resources issues, including labour relations and pensions. Where appropriate, we will comment on proposals that apply to various sectors of the BPS.

THE DRUMMOND REPORT

The Budget comes on the heels of the report of the Commission on the Reform of Ontario's Public Services (the "Drummond Report"), which was released on February 15th of this year. In the Drummond Report, the Commission recommended sweeping reform measures to apply to all sectors of the BPS in an effort to achieve a balanced budget within the Government's stated timelines. Hicks Morley summarized the recommendations contained in the Drummond Report in two previous issues of *FTR Now:* The Drummond Report – Impact on the Broader Public Sector*;* and Drummond Commission Reports on Elementary and Secondary Education Reform*.* The Budget adopts a significant number of the recommendations made in the Drummond Report, though quite a few key recommendations were not incorporated.

BROADER PUBLIC SECTOR COMPENSATION AND LABOUR RELATIONS – GENERAL

The Budget and Bill 55 contain numerous proposals on public sector compensation, which would have an impact on employers in the BPS generally. Many of the proposals relate to public sector pensions and executive compensation, and those are considered in separate sections of this *FTR*

Now. In this section, we will consider some of the proposed changes of more general application.

WAGE FREEZE

Based on our review of the Budget and Bill 55, it appears that the general wage freeze for non-union employees in the BPS will expire on March 31, 2012 as provided for in the *Public Sector Compensation Restraint to Protect Public Services Act, 2010*. However, as discussed in the section on Executive Compensation, below, a wage freeze will continue for a further two years for certain high level executives in the BPS.

Moreover, the Budget strongly signals the Government's intention to negotiate a two-year wage freeze for unionized employees in the BPS. This is expressly described with respect to teachers and other school board employees, and is considered in greater detail, below, in the "School Boards" section of this *FTR Now*. However, the Budget document indicates that the Government will pursue a "very similar mandate" (i.e., as that being negotiated with the school board unions currently) with other areas of the BPS. Media reports suggest that this would include hospital workers, amongst others. Similarly, the Government suggests that its bargaining strategy will apply to its upcoming negotiations with the Ontario Public Service.

The Budget also indicates that if the Government is not able to secure wage restraint goals through the collective bargaining process, the Government will consider other means to achieve them, including passing legislation that would mandate the desired results.

COLLECTIVE BARGAINING AND INTEREST ARBITRATION

Consistent with its wage restraint goals, the Budget does not include any funding for incremental compensation increases for new collective agreements. In addition, the Government has signalled the need for BPS employers to negotiate provisions that would increase productivity and enhance public-sector transformation.

In terms of collective bargaining generally, the Budget sets out a number of proposals of interest to BPS employers. First, the Budget calls for the Government to explore the possibility of greater centralization of collective bargaining in order to save on the costs associated with negotiating thousands of individual collective agreements.

Second, the Government intends to amend the interest arbitration process to:

- require written submissions from the parties to the arbitration;
- require written rationales from the arbitrator at either party's request;
- create a 12-month time limit on the issuance of an arbitration award (subject to limited extension in exceptional circumstances); and
- permit the Ontario Labour Relations Board to issue an award if the arbitration award is not

rendered in a timely fashion.

Bill 55 proposes amendments to a variety of statutes that incorporate interest arbitration consistent with these principles – for example, the *Ambulance Services Collective Bargaining Act, 2001,* the *Fire Protection and Prevention Act, 1997*, the *Hospital Labour Disputes Arbitration Act* and the *Police Services Act,* amongst others.

Third, the Government has indicated that it will initiate a dialogue with employers and other parties to facilitate collective bargaining and the interest arbitration process. The Government proposes to consult with employers who have large numbers of employees who are subject to interest arbitration about "additional tools they may need to live within their funding envelopes while protecting services." In addition, the Government has proposed wider consultations with employers, bargaining agents and other stakeholders on additional tools they might need to operate within their funding allocations.

EXECUTIVE COMPENSATION

As noted above, the Budget proposes a new two-year wage freeze for executives of certain BPS organizations. Bill 55 clarifies that the wage freeze would be accomplished through amendments to the *Broader Public Sector Accountability Act, 2010.* Highlights are set out below.

First, the wage freeze would apply to "executives" at the following BPS organizations: public hospitals (including the University of Ottawa Heart Institute); school boards; universities and colleges; Hydro One; the Independent Electricity System Operator; Ontario Power Authority; and Ontario Power Generation. Other BPS organizations could be added by regulation.

"Executive" is defined as any of the following individuals who make at least $100,000 in compensation on an annualized basis: the head of the organization (whatever his or her title); a full-time member of the board; a vice president, chief administrative officer, chief operating officer, chief financial officer, chief information officer or other similar executive; a director of education or superintendent of a school board; or the provost or dean of a university or college.

The wage freeze would incorporate a complete freeze on base salary to the level in effect on March 31, 2012 (or other applicable effective date), with no movement permitted through salary grids. With limited exceptions, there would be a general freeze on bonuses, benefits and perquisites. For example, new or increased performance pay and other forms of compensation would need to be tied to meeting certain defined performance standards and be authorized under existing compensation plans.

Furthermore, the Government would be empowered to issue directives requiring these BPS employers to conduct compensation studies to establish the compensation levels payable to the executives.

PENSION, BENEFITS AND TAX ISSUES

In the next few sections of the *FTR Now*, we will consider the significant proposals related to pension reform before turning to some sector-specific analysis.

BROADER PUBLIC SECTOR PENSIONS

The Budget contains proposed measures to improve the sustainability and efficiency of these public sector and BPS plans without adding further cost to taxpayers. These proposed measures will affect jointly sponsored pension plans and single-employer pension plans in slightly different ways. A third measure seeks to encourage pooling of investments to reduce expenses and improve returns.

1. BROADER PUBLIC SECTOR: JOINTLY SPONSORED PENSION PLANS ("JSPPS")

Most of Ontario's largest pension plans are JSPPs – e.g., Ontario Teachers' Pension Plan, OMERS and the Healthcare of Ontario Pension Plan. The Government wants all JSPPs to transition to a 50-50 funding cost sharing formula between employers and employees. The Government will consult with its partners and stakeholders to develop a legislative framework for JSPPs taking into account the following key parameters, amongst others:

- if the JSPP has a funding deficit, future benefits must be reduced before employer contributions are increased – in exceptional circumstances, some limit may be placed on the size of the reductions;
- benefits reductions will be in respect of future benefits only (retirees would not be affected);
- if the plan sponsors cannot agree on reductions through negotiation, the disagreement will be resolved through a third party dispute resolution process; and
- employee contributions could be increased if they are less than employer contributions.

2. BROADER PUBLIC SECTOR: SINGLE-EMPLOYER PENSION PLANS ("SEPPS")

Many public sector employees participate in SEPPs, particularly in the university and electricity sectors. The Government believes that employers and members of these SEPPs should share equally in the ongoing cost of their pension benefits. The Government expects SEPPs to transition to the 50-50 ongoing cost-sharing funding model within five years. In the interim, the Government will adjust temporary solvency relief measures to encourage implementation of this cost sharing within the five-year transition period.

The Government also intends to support the conversion of existing BPS SEPPs into JSPPs with full equal cost-sharing and, to this end, will remove a current barrier to the creation of new JSPPs specific to the energy sector (see section 102 of the *Electricity Act, 1988*).

3. BROADER PUBLIC SECTOR: PENSION ASSET MANAGEMENT

To take advantage of economies of scale and reduce duplication of costs, the Government intends to introduce a legislative framework in the fall of 2012 that would facilitate the pooling of the assets of Ontario's smaller defined benefit public-sector pension plans either through a new investment management entity or by building on the structure of existing large public-sector pension plans. The Government will appoint an advisor to lead the implementation process.

ONGOING PENSION REFORM

In 2010, the Government introduced two reform packages. In previous issues of *FTR Now*, we summarized the key provisions of these packages – Implementing Phase One of Ontario Pension Reform: A Roadmap for Plan Sponsors and Administrators (May 19, 2010) and *Ontario Introduces Bill 120, The Securing Pension Benefits Now and for the Future Act, 2010* (October 29, 2010). Most of these prior reform measures have not yet been proclaimed into force.

However, in the Budget, the Government confirmed that it intends to proclaim the following provisions of the past initiatives in force effective July 1, 2012:

- the elimination of partial wind-ups;
- immediate vesting of pension benefits;
- the availability of grow-in benefits to all eligible members terminated for reasons other than cause-like misconduct and an election for multi-employer pensions plans and jointly sponsored pension plans to opt out of providing these grow-in benefits.

The Government also confirmed that regulations are currently being drafted to support many of the measures stemming from the 2010 pension reform packages. In particular, later this spring the Government intends to post draft regulations that would clarify pension surplus rules, implement the asset transfer provisions, and implement provisions regarding the rights and responsibilities of retired plan members. Draft regulations will follow later in 2012 to provide a "funding concerns" test for plans not required to fund on a solvency basis, and to strengthen funding rules for defined benefit pension plans.

Many of these measures will require employers to take action this spring in anticipation of the legislative and regulatory changes that will be effective July 1, 2012.

PRIVATE SECTOR: SOLVENCY FUNDING RELIEF AND ADDITIONAL FUNDING FLEXIBILITY

The Government proposes to extend temporary solvency funding relief measures for private sector defined benefit plan sponsors. The proposed solvency relief is an extension of the 2009 solvency funding relief regulations. This means that when the first actuarial valuation report dated on or after

September 30, 2011 is filed, a plan administrator will be able to consolidate existing solvency payment schedules into a five-year payment schedule and, with member consent, extend the solvency payment schedule to a maximum of ten years for any new solvency deficiency identified in the report.

To reduce cash-flow pressures on employers required to make lump sum catch up special payments after a valuation report is filed, the Government reiterated that it will introduce regulations permitting solvency and going concern special payments to be amortized beginning one year after a plan valuation date, or, in other words, delay new special payments by one year. Regulations that permit employers to use irrevocable letters of credit issued by financial institutions to cover up to 15% of a plan's solvency liability (as announced in August 2010) will also be put in place. This measure would provide employers with flexibility to manage their financial resources by only requiring them to fund up to 85% of their plan's solvency liabilities. Both of these measures were previously introduced when Bill 120 was announced in August 2010.

FINANCIAL HARDSHIP UNLOCKING

Pension benefits that have been transferred out of a pension plan to a locked-in retirement savings vehicle, such as a LRIF, LIF or a LIRA, may be unlocked by a former member in limited circumstances. The current process for unlocking an account requires an applicant to apply for the consent of the Superintendent of Financial Services ("Superintendent"). The Government intends to restructure the unlocking process by no longer requiring an applicant to seek the consent of the Superintendent prior to unlocking his or her pension benefits. Instead, applicants will have to make a request for the withdrawal of locked-in funds from their financial institution.

Bill 55 introduces the amendments to the *Pension Benefits Act* ("PBA") needed to implement this change.

BILL 55 TECHNICAL AMENDMENTS TO THE PBA

Bill 55 makes several technical amendments to the PBA to clarify previous amendments made in previous reform Bills that have not yet come into force, such as changes to the definition of "pension benefit" to take into account retired members and changes to section 44 (joint and survivor pension benefits) and 79.1(2) (defined contribution asset transfers) to clarify prior amendments to these sections in previous Bills.

Bill 55 also amends section 72 (notice of entitlement upon wind up and election) of the PBA to enable the Superintendent to require the plan administrator to give specified additional information and documents to those entitled to a wind up statement.

UNCLAIMED INTANGIBLE PROPERTY

The Government intends to establish an Unclaimed Intangible Property Program ("Program"). Intangible property, which will include, amongst other things, insurance policies, unpaid wages, and pension benefits, will be held by the Program until the owners of the property can be located. While the property remains unclaimed, the value of the intangible property will be used "for the benefit of Ontarians." Although no details of the Program have been released, it is hoped that the Program will provide plan administrators with an alternative to retaining responsibility indefinitely for pension benefits of former plan members who cannot be located.

GOVERNMENT SUPPORTS ENHANCED CANADA PENSION PLAN ("CPP")

The Budget reaffirmed the Government's support of improving the retirement income system through a "modest, phased-in and fully funded" enhancement to the CPP. It considers this change to be the core element of an effective national retirement income system strategy. The Government supports a fully funded CPP enhancement under which employees and their employers would pay for the additional benefits as they are earned. The Government's version of a CPP enhancement would be fully implemented over a 40-year period, with gradual, phased-in changes to the contribution rates.

The Government intends to continue collaborating with other provinces and the federal Government to develop a plan to enhance the CPP in a way that is predictable and manageable for employers and employees.

CONCERNS RAISED REGARDING POOLED RETIREMENT PENSION PLANS ("PRPPS")

In late 2011, the federal Government introduced Bill C-25, the *Pooled Registered Pension Plans Act,* applicable to federally regulated employees, and proposed amendments to the *Income Tax Act (Canada)* to enable the establishment of PRPPs. See our *FTR Now* on *Bill C-25, Pooled Registered Pension Plan Framework Introduced,* for more details. A PRPP is an occupational defined contribution pension scheme administered by a financial institution, not the employer, and it is intended to increase pension coverage.

The Ontario Government revealed in the Budget that it has a number of concerns with the federal PRPP model as currently proposed. These concerns are rooted in its desire to focus on the protection of members in a for-profit environment, including whether: (i) PRPPs will actually expand retirement savings and coverage; (ii) the fiduciary framework for PRPPs will adequately protect plan members; (iii) the compulsory employee contributions would be flexible enough to allow for member life events; (iv) PRPPs could achieve their low-cost objective; and (v) the costs of provincial regulation of PRPPs will be reasonable.

The Government's announcement comes on the heels of the Quebec Budget last week in which a mandatory retirement scheme was introduced for all employers with five or more employees.

INCOME-TESTED ONTARIO DRUG BENEFIT (“ODB”) DEDUCTIBLES

The ODB program provides prescription drug coverage for Ontarians aged 65 and older. Under the current ODB program, eligible seniors pay the first $100 of their drug costs each year and a co-payment of $6.11 for each prescription after the $100 deductible. For low income individuals, the deductible is waived and the co-payment is reduced to $2.00.

Beginning in August 2014, single high income seniors will pay an additional deductible amount equal to 3% of their income over $100,000 in addition to the existing $100 deductible. A similar income-tested additional deductible will apply to couples with incomes exceeding $160,000. Incomes will be checked each year, but the thresholds will not increase with inflation. Seniors living in long-term care homes or receiving publicly-funded home care are not affected.

These changes to ODB could have implications for employers who provide drug benefit coverage for employees working past age 65 or retirees whose income exceeds $100,000.

EMPLOYER HEALTH TAX (“EHT”)

As part of its Budget commitment to enhance revenue integrity and minimize tax leakage, the Ministry of Finance will no longer automatically follow federal Canada Revenue Agency rulings on whether an employer-employee relationship exists. This could result in a worker being treated as an independent contractor for federal purposes (including CPP and EI) but as an employee for EHT remittance purposes, triggering an obligation on the paying entity to remit EHT on the compensation paid to the worker. The change in practice will apply to EHT assessments issued after March 27, 2012.

SECTOR-SPECIFIC PROPOSALS

In the final few sections of this *FTR Now*, we will consider Budget proposals that are specific to various sectors of the BPS.

SCHOOL BOARDS

The Budget proposals contain significant changes for school boards, some of which were considered in the Drummond Report while others have been made known since the release of that Report. The following is a summary of a number of the key proposals.

First, the Government has rejected some of the more controversial Drummond Report recommendations, and confirmed that full-day kindergarten will be fully implemented province-wide by September, 2014. Moreover, the Government has proposed to maintain funding to preserve current caps on primary class sizes, as well as existing average class sizes at the junior and senior levels.

Second, the Budget includes a number of cost-saving measures, many of which focus on the Government's ongoing labour negotiations with the various school board unions. Those measures, which are consistent with the parameters presented by the Government to the various unions and school board associations in the recent discussions regarding provincial bargaining in the school board sector, include:

- a two-year wage freeze with no incremental increases on the salary grid;
- a freeze on banked sick days accumulated to August 31, 2012 – upon retirement, any gratuity payout would be based on 2012 salary rates, while all accumulated non-vested sick days would be eliminated as of September 1, 2012;
- a new short-term disability plan that offers six sick days per year at full salary and 24 weeks at 2/3 salary (with no carryover); and
- negotiating over the future viability and solvency of the Ontario Teachers' Pension Plan without increasing government contributions or negatively affecting the province's fiscal plan.

If the Government is not able to secure these goals through the collective bargaining process, the Budget states that the Government will "consider all options to meet its fiscal goals, including intervention through legislation or other means."

Other proposed changes in the school board sector include changes in school board allocations to encourage school boards to consolidate underutilized schools (a measure that would result in school closures), and the amalgamation of school boards in areas of the province with low population growth and declining enrolment.

HEALTHCARE

At the outset of this *FTR Now*, we discussed a number of general proposals related to BPS compensation and labour relations generally, including changes to the interest arbitration process and the Government signalling that the BPS should be negotiating two-year wage freezes with its unionized workforces. Clearly, these issues will be highly relevant to the healthcare sector.

Uniquely to the healthcare sector, the Government has proposed a freeze on total physician compensation at current levels through the next Physician Services Agreement with the Ontario Medical Association.

In addition, many of the Government's proposed cost-saving measures in the healthcare sector are premised on the downloading and transfer of healthcare services from higher cost service providers (such as hospitals) to lower cost community care providers. As we discussed in our review of the Drummond Report, any efforts at transferring health services or consolidating or integrating services or service providers may well engage the successor rights provisions of the *Public Sector Labour Relations Transition Act*, which could significantly limit any cost-savings that might otherwise be achieved. Moreover, many health sector collective agreements contain restrictions on contracting out, the reassignment of duties, staffing ratios, etc., which might be engaged by the proposed restructuring.

MUNICIPALITIES AND SOCIAL SERVICES

As with organizations in the healthcare sector, municipalities and organizations in the social services sector will also have an interest in the general labour relations and compensation proposals set out in the Budget, and discussed at the outset of this *FTR Now*.

In addition, for municipalities, the Government has committed to maintaining its uploading of services as agreed to through the Provincial-Municipal Fiscal and Service Delivery Review of 2008, which should be complete by 2018. In the social services sector, the Budget indicates that the Government is planning to continue its amalgamation initiative for children’s aid societies.

CONCLUDING COMMENTS

As has been evidenced in our preceding review, there are many proposals in the Budget that have the potential to significantly alter employment relationships in the BPS, including significant changes to collective bargaining and public sector pensions. Other provisions, such as the cancellation of planned business tax reductions, will have an impact on all employers in Ontario.

We would be remiss not to consider the potential impact of the current minority parliament situation that exists in the Legislature. Ordinarily, Budget Bills can be expected to pass as they are necessarily confidence measures – if the Budget does not pass, a government will fall. Because the McGuinty government is a minority government, there is a real possibility that the Budget will either not pass or will pass in an amended form (if changes are needed to ensure the support of one of the opposition parties). When reviewing the Budget and Bill 55, and considering the impact that they will have on your organization, it is important to keep in mind that changes could still happen before the Budget is finalized.

We will continue to monitor any changes to the Budget and to Bill 55, and will inform our clients of any significant amendments. In the meantime, if you have any questions about the Budget, please feel free to contact any of the authors of this *FTR Now* or your regular Hicks Morley lawyer.
