FTR Now

Ontario Moves Forward with BPS Executive Compensation Restraint

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The countdown is on: new process and one-year timeline now in place for the development of executive compensation programs by Broader Public Sector (BPS) organizations.

On September 6, 2016, the Ontario government published Ontario Regulation 304/16 “Executive Compensation Framework” (Regulation) under the *Broader Public Sector Executive Compensation Act, 2014* (BPSECA), which provides the compensation framework in accordance with which compensation programs for “designated executives” under the BPSECA must be developed, including a detailed process and specific one-year timeline for their development.

The Regulation, which also prescribes what can and cannot be included in the compensation plans of designated executives, is now in force – however, existing compensation restraint obligations under Part II.1 of the *Broader Public Sector Accountability Act, 2010* (BPSAA) continue to apply until BPS organizations establish new compensation programs in accordance with the new process, which can be no later than September 5, 2017.

In addition to the Regulation, the government published the Executive Compensation Framework Guide (Guide), which sets out further guidance on the development of the required compensation programs.

In this *FTR Now*, we provide an overview of the Regulation, how it interacts with existing compensation restraint obligations under the BPSAA, how it is likely to impact organizations in the Ontario BPS – and what steps affected BPS organizations should be taking to achieve compliance.

Background to the BPSECA

As we reported in our *FTR Now* of March 10, 2015, New BPS Compensation Restraint Law to Come into Force March 16, the BPSECA came into force in 2015 and will eventually replace the current compensation restraint measures contained in Part II.1 of the BPSAA.

Part II.1 of the BPSAA essentially imposed a complete compensation freeze on the “designated executives” of a wide range of BPS organizations – hospitals, school boards, colleges and universities along with certain other post-secondary institutions, Hydro One and its subsidiaries, Ontario Power Generation and its subsidiaries, and the Independent Electricity System Operator. The BPSECA replaces the BPSAA compensation freeze with a “compensation framework,” the details of which are contained in the Regulation.

Application of the BPSECA

The BPSECA applies to a wide variety of BPS organizations, including most of the BPS organizations currently subject to Part II.1 of the BPSAA (except for Hydro One, which is covered by Part II.1 of the BPSAA, but not the BPSECA). In addition, numerous organizations that were not subject to Part II.1 of the BPSAA are covered by the BPSECA and its compensation framework – all community care access corporations (CCACs), Ornge and all organizations prescribed as public bodies under the *Public Service of Ontario Act, 2006* that are not also prescribed as Commission public bodies.

Like the BPSAA before it, the BPSECA only applies to “designated executives” who earn at least $100,000 on an annualized basis. This group includes:

- the head of the organization, regardless of title
- a vice president, chief administrative officer, chief operating officer, chief financial officer, chief information officer or other executive, regardless of title
- a director of education or supervisory officer of a school board.

Unlike the Part II.1 of the BPSAA, the BPSECA does not specifically list the “dean or provost” of a college or university in the definition of “designated executive.” Therefore, employees holding these positions are only subject to the BPSECA and its compensation framework if they hold what would be considered an “executive” position in their organization.

In addition, the BPSECA retains a feature common to all of the prior compensation restraint statutes – namely, that it does not apply to any designated executives who collectively bargain terms and conditions of employment related to compensation.

General Operation of the Framework

The Regulation applies to all BPS organizations that are subject to the BPSECA and is now in force. It requires each affected organization to develop written compensation programs that set out what compensation may be provided to its designated executives. The compensation programs are to be developed in accordance with the framework set out in the Regulation. They must include certain specified information, including the maximum salary and performance-related pay for each designated executive or class of designated executive positions, information related to how those amounts were arrived at, a description of certain other amounts of compensation provided to designated executives, and the organization’s “compensation philosophy.”

Once developed, the compensation program must be published on the organization’s website, and it is on this date that the Regulation deems the “compensation framework” to be effective. We will explain the implications of this below.

The Regulation requires affected BPS organizations to engage in public consultations that provide members of the public a reasonable opportunity to provide comments on the manner in which the organization determines the compensation that it will be paying to its designated executives.

The Guide provides more details on what the government expects in terms of the public consultations, and states that BPS organizations will be required to post the draft compensation programs for at least 30 days on their public-facing websites, and to establish a process for collecting feedback in response (a separate process applies to government agencies with existing government approval mechanisms for executive compensation).

Specific Terms of the Compensation Framework

The Regulation establishes the requirements of the framework under which the compensation of designated executives is to be calculated. These include:

- a cap on salary and performance-based compensation along with requirements on when salary and performance-based compensation may, or in some cases, must be recalculated
- the identification of types of compensation that cannot be part of a compensation plan (subject only to entitlements that may arise under the *Employment Standards Act, 2000*), including:
    - payments or benefits in lieu of perquisites
    - signing bonuses
    - retention bonuses
    - cash housing allowances
    - insured benefits if the benefits are not generally provided to “non-executive managers” (defined as employees or office holders who exercise managerial functions and who directly report to a designated executive)

- termination and severance payments of more than 24 months times the average monthly salary
- paid administrative leave – except to the head of a college or university or other designated executive who will return to the faculty of a college or university
- paid administrative leave that accrues at more than 10.4 paid weeks per year
- payment in lieu of administrative leave
- restrictions on when compensation can include elements beyond salary and performance-related compensation (generally considered with reference to what is paid to “non-executive managers” unless a proscribed business case can be made)
- limits on how salary increases may be provided to designated executives (requiring board/governing body approval and tied to increases provided to “non-executive managers”).

The Regulation provides a detailed process by which affected BPS organizations can determine the maximum salary and performance-related compensation that may be provided to designated executives. The process involves the identification of at least eight comparator organizations, and calculating salary and performance pay at no more than the 50th percentile of what is paid to executives holding comparable positions in those comparator organizations.

At least one of the comparator organizations must come from the Ontario BPS or Canadian public sector. However, organizations that want to use comparators from the private sector or from outside Canada will need the prior consent of the responsible Minister (President of Treasury Board) in order to do so.

It should be noted that the Regulation gives BPS organizations one year to complete this process, including the public consultations, as the finalized compensation program must be published no later than September 5, 2017.

Continued Application of the BPSAA

As noted above, the “compensation framework” is deemed to be effective only when an organization has completed the development of a compensation program as required by the Regulation, and has published the program on its website.

This timeline is important because, for organizations currently covered by Part II.1 of the BPSAA, that Part will continue to apply to the organization until the BPSECA process has run and the compensation program is published. Therefore, notwithstanding that the Regulation is now in force, Part II.1 of the BPSAA continues to apply and will do so for some time still.

Impact on Designated Executives

Once the compensation framework is deemed effective, it will begin to apply to all designated executives. However, different rules apply if a designated executive is hired on or after the effective date, or if the designated executive is already employed in a designated executive role on the effective date.

Designated executives who are hired on or after the effective date of the compensation framework will be immediately subject to its restrictions and their compensation plans must be in accordance with its terms.

Designated executives who are employed prior to the effective date of the compensation framework will be subject to the new framework, but section 9 of the BPSECA has the effect of grandparenting any non-compliant aspects of their compensation plan for a period of three years from the effective date. That is, an organization may continue to pay compensation in excess of, or that would otherwise not be permitted under, what is allowable under the framework for three years from the effective date. Once this three-year grandparenting period comes to an end, the BPSECA makes it clear that any non-compliant elements of the compensation plan are neither valid nor payable.

Note that this three-year grandparenting period will cease to apply if an existing designated executive accepts a new

designated executive role during the three-year period (e.g. a Vice-President accepts a promotion to President). In that case, the restrictions of the framework will begin to apply immediately upon the designated executive assuming the new role.

The impact of these provisions means that for a period of up to three years, an organization might have designated executives employed under different compensation plans during the grandparenting period, and that adjustments to executive compensation may be legislatively imposed after the grandparenting period has ended.

Next Steps

All BPS organizations subject to the BPSECA will want to begin planning how they will develop a compensation program in compliance with the framework set out in the Regulation, and should carefully review the Regulation and consult the Guide for details on what the government expects that they will do.

Organizations will also want to begin considering what are their comparator organizations for the purposes of developing salary and performance-related pay amounts. While the Regulation establishes criteria that organizations must consider in choosing comparators, this is a strategic question and should also be considered in light of an organization's overall compensation strategy.

Another area requiring consideration is determining who are the "designated executives" that fall within the BPSECA, and who are the "non-executive managers" that are to be used in determining the applicable elements of the compensation program.

Our lawyers are well-positioned to assist clients with navigating the BPSECA and the requirements of the Regulation. If you have questions about these issues or for further guidance, please contact your regular Hicks Morley lawyer.

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