

Case In Point

Notice of Intended Decision Considers Whether Vacation Pay Forms Part of Pensionable Earnings

Date: March 4, 2019

The Ontario Superintendent of Financial Services (Superintendent) issued a [Notice of Intended Decision](#) (NOID) in late 2018 that considered whether vacation pay should be factored into a pension plan's definition of pensionable earnings. The NOID indicates that, in the absence of clear exclusionary language, the Superintendent will interpret the phrase "base pay" to include vacation pay. Like all NOIDS, the NOID is not binding law but is a clear statement of the Superintendent's position on the matter.

At issue was a defined benefit accrual formula in a plan (Plan) that was partly based on each Plan member's "final average earnings" (FAE). The Plan defined FAE as including:

"'base pay' and eligible commissions",

but excluding:

"bonuses, overtime pay, and any other forms of compensation", and

taxable benefits in respect of any stock options exercised.

Upon retirement, a member of the Plan (Member) complained that the lump sum payment of vacation pay he received at his termination of employment was not included in the determination of his FAE, resulting in a lower overall Plan benefit.

The Plan's administrator (Administrator) took the position that its practice of excluding lump sum payments of vacation pay at termination of employment from the determination of FAE was a reasonable interpretation of the Plan terms. The Administrator argued that because the lump sum payment represented unused vacation time, including it in the Member's FAE would amount to "double counting."

The Superintendent disagreed with the Administrator's interpretation of the Plan terms. The NOID notes that "[t]he Plan does not define 'base pay'". However, in the Superintendent's view, "vacation pay is an integral part of base wages and is not a separate amount that is earned through bonuses or stock options." Further, the Superintendent was of the view that vacation pay should be included in "base pay" since the Plan terms do not explicitly exclude it and because the Ontario *Employment Standards Act, 2000* provides that vacation pay accrues during employment, as a matter of minimum standards. As a result, the lump sum represented payment of an amount (i.e., unused vacation time) that was owing to the Member on termination.

The NOID does not make it clear whether the Administrator factored vacation pay that was not paid as a lump sum into the determination of FAE. Regardless, in failing to factor all forms of vacation pay into the Member's FAE, the Superintendent determined that the Plan was not being administered in accordance with its terms. Therefore, the Superintendent issued the NOID directing that the Administrator factor vacation pay into the determination of the Member's FAE.

The NOID is good reminder of the importance of drafting pension plan texts to clearly outline what is included and excluded from defined terms. While using general terms to describe remuneration is not an uncommon approach to defining "earnings" in a pension plan text, using specific exclusions can help ensure that a plan is interpreted and administered in accordance with the plan sponsor's intentions.



Note that a hearing has been requested before the Financial Services Tribunal to appeal the NOID. We will continue to monitor this case.