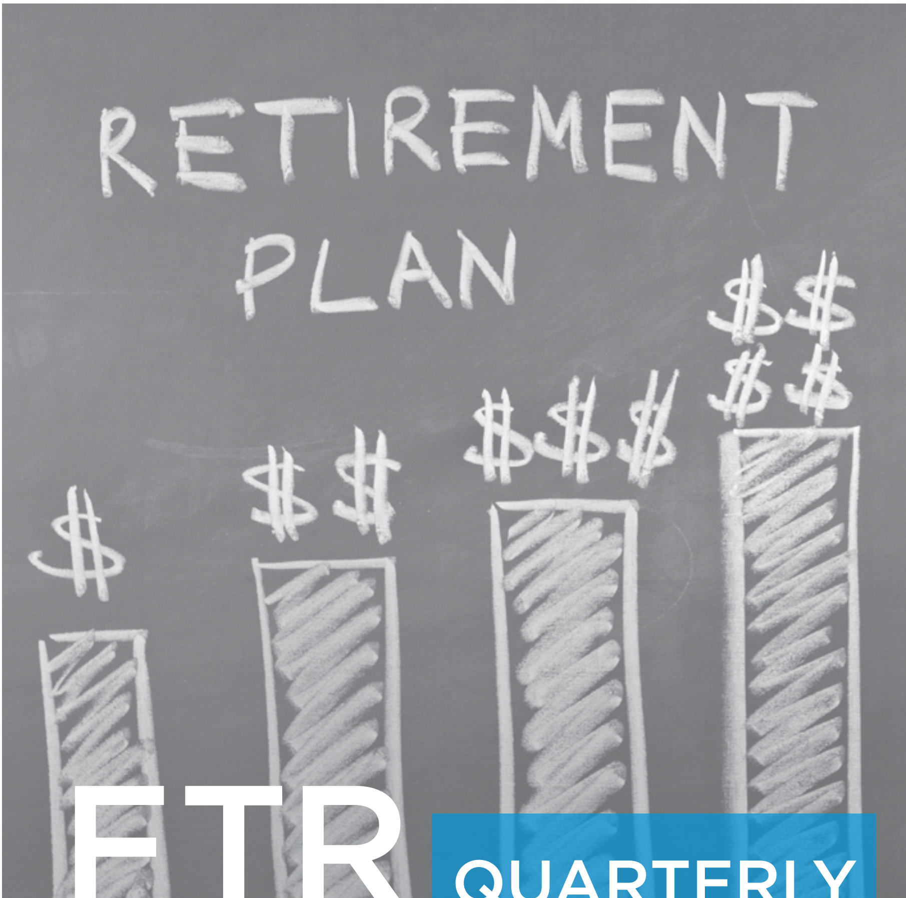

FTR QUARTERLY

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In this issue:

Hicks Morley

HUMAN RESOURCES
LAW AND ADVOCACY

RECASTING THE PENSION PROMISE

Times have changed in the pension world. While defined benefit ("DB") pension plan deficits and unfunded liabilities existed many years before the economic meltdown of 2008, the last quarter of 2008 was a turning point. Within a few short months, what used to be the exception became the norm – and DB plan deficits became virtually universal.

"Since the downturn, we continue to see Canadian and global employers in both the private and public sector focusing on ways to cut costs," says Terra Klinck, a partner in the Hicks Morley Toronto office. "There's a continued move from DB to defined contribution ("DC") plan designs – and employers who continue their DB plans are looking at a number of strategies for managing the deficits, from increasing employee contributions, to decreasing benefit levels, to looking at more fundamental changes to plan design such as target benefit plans."

INNOVATION CAN BE THE ANSWER

When it comes to larger plan issues – such as deficit funding – an innovative approach to long-term solutions is often needed. And legislative changes are helping this to happen.

"Governments across the country have instigated the most significant pension reform in a generation – and these have given us some new tools to fashion new types of pension arrangements," says Elizabeth Brown, a Toronto office partner and Chair of the firm's Pension, Benefits and Executive Compensation Practice Group.

One of these is the target benefit plan, which fixes pension contributions at specified levels while targeting particular benefit levels. The benefits are only "targets" since they are subject to reduction if plan funding levels are not sufficient to provide for them. But there are other changes occurring as well.

"We have worked with clients to implement or revise jointly sponsored pension plans, where plan members and the employer share deficits," says Brown. "We also have worked on innovative arrangements to freeze escalating employer contributions through agreements to modify benefit levels before resorting to contribution increases."

These solutions aren't just designed for non-union employers – change and innovation is also taking place through the collective bargaining process.

"We've helped employers to bargain the closing of DB plans, increased member contributions, and the elimination of expensive early retirement subsidies and indexation," says Brown. "And in some cases, we've assisted our clients to establish bargained contingency arrangements so that when funding levels improve, negotiated changes can be restored."

CONFLICTS EMERGING

As pension resources grow scarcer, one of the other side effects is a rise in disputes.

"The pension world has become more litigious than ever," says Sean Sells, an associate in the firm's Toronto office. "We're resolving pension-related disputes at the bargaining table, in the courts, before mediators and arbitrators, in hearings at the Financial Services Tribunal, the Human Rights Tribunal – the list goes on."

One of the key areas with potential for disputes is in the human rights arena. These issues can arise at the time of a plan launch or change, or flow from the decision of an employer or plan administrator in interpreting plan rules, or can arise out of the application of historical plan provisions around eligibility.

As pension resources grow scarcer, one of the other side effects is a rise in disputes.

"We've really seen an increase in the number of pension matters in which human rights considerations come into play and sometimes these claims can create discrimination claims," says Sells.

THIS TIME IT'S PERSONAL

Another form of dispute that is on the rise is conflicts between potential beneficiaries. Pension benefits often represent one of the most significant family assets, and when a plan member dies, family situations and entitlements are often far from clear and may lead to litigation involving the plan administrator or sponsor.

"We're seeing an increased willingness to dispute entitlement to death benefits when a plan member dies," says Natasha Monkman, an associate in the Hicks Morley Toronto office.

"Unfortunately, sponsors and administrators are increasingly finding themselves in the middle of family disputes following a member's death – whether between former and current spouses or a spouse and the member's children. More than ever, it's important for sponsors or administrators to have sound and consistent administration processes to help avoid these types of issues."

PENSIONS ABHOR A VACUUM

Organizations can no longer deal with pension plans in isolation because the issues they raise cross an entire spectrum of concerns. For example, the recent Supreme Court of Canada decision in *Sun Indalex LLC* highlights a need for employers to be up to date on their fiduciary duties to plan members even when engaged in corporate, not pension, decision making. From finance, to human rights, to collective bargaining, pensions intersect and must be understood in a context.

"It's one of our key differentiators as a firm – our lawyers understand, appreciate and can advise on the labour relations and employment law aspects of the bigger picture when it comes to pensions and benefits," says Rachel Arbour, an associate in the firm's Toronto office.

These are challenging times for all pension plans, with persistent low, long-term interest rates, an aging demographic, and a proliferation of plant closures and corporate insolvencies. But innovative solutions exist – and expert advice and a 360-degree perspective on how a plan fits into larger operational goals can provide lasting value to all organizations, no matter what type of pension or retirement arrangement they maintain for their employees.

From finance, to human rights, to collective bargaining, pensions intersect and must be understood in a context.

HR QUICK HITS

Leave to appeal in *Carrigan* denied, pension administration changes required

The Supreme Court of Canada has denied leave to appeal from a decision of the Court of Appeal for Ontario (*Carrigan v. Carrigan Estate*) regarding the administration of pre-retirement death benefits under section 48 of the Ontario *Pension Benefits Act* ("PBA"). The Court of Appeal fundamentally altered the prevailing interpretation of spousal rights and priorities relating to payment of pre-retirement death benefits by awarding the pre-retirement death benefit payable under an Ontario registered pension plan to a member's designated beneficiaries instead of his common-law spouse.

The outcome of this case is contrary to what Ontario pension plan members may have been told about spousal priorities on communications such as enrolment forms, beneficiary designation forms, plan booklets and Internet sites. Plan administrators will want to consider bringing the implications of *Carrigan* to the attention of their active and deferred plan members and to review existing forms and communications to determine whether they need to be re-worded. Any member of our Pension, Benefits and Executive Compensation Practice Group would be pleased to discuss the decision with you and how to communicate its impact to your plan members.

PAY FOR PERFORMANCE: PROVIDING KEY EMPLOYEES THEIR JUST DESSERTS

Boards and senior management are responsible for implementing incentives that encourage key employees to innovate, take appropriate risks and invest the hard work required to realize sustainable gains for investors and stakeholders. Restrictive tax rules and other considerations can complicate this task.

BY: JOHN PREZIOSO

A REAL SLICE OF THE PIE

The watchword in incentive compensation is "alignment" – the notion that organizational gains yield compensation for the individual, whereas exposing the organization to risk puts individual compensation at risk. One means of promoting alignment is to grant employees an equity stake. Broad-based share ownership plans have long been a tool used by public companies to align individual and corporate interests. Increasingly, "C-level" executives are being asked to maintain a minimum level of share ownership throughout the term of employment.

Given their favourable tax treatment in Canada, stock options are another popular means of facilitating key employees' acquisition of equity. Provided that the fair market value of the optioned shares ("FMV") on the grant date is not higher than the exercise price ("EP"), the optionee is not taxed until the options are exercised, at which time the stock option benefit (FMV minus EP) is included in the optionee's income. If the underlying shares are in a Canadian-controlled private corporation, tax on the stock option benefit is generally deferred until the shares are sold. If certain other conditions are met, the optionee can deduct 50% of the stock option benefit.

If options become significantly "under water" they cease to incent. Further, "at-the-money" options can encourage optionees to take risks to increase the share price but the optionee does not bear corresponding risk if the share price drops, since his/her options will simply lapse. For these reasons, options have been criticized for their potential to misalign organizational and individual interests.

Popular in the United States where grants enjoy favourable tax treatment, restricted stock is generally not an appropriate incentive for Canadian employees except in limited circumstances because grants are taxed immediately even though the shares may later be forfeited.

NOTIONAL EQUITY COMES IN A VARIETY OF FLAVOURS

"Notional equity" plans may be an appropriate incentive compensation vehicle where it is not desirable or possible to grant real equity. Under Canadian tax rules, deferred compensation is taxed immediately at grant unless an exception applies. Notional equity plans must be designed carefully to ensure participants are not hit with tax on amounts they haven't yet (and may never) receive.

A key exception to immediate taxation permits the deferral of bonus payment for up to three years. Instead of a fixed dollar amount, bonuses can be granted in phantom shares – either restricted

	Incentive	Description	Horizon
Cash	Cash Bonus	Cash payments tied to corporate or individual performance	Short/Mid
Notional Equity	Stock Appreciation Rights ("SARs")	Right to a cash payment equal to the increase, if any, in share price after the grant date. Can be settled in shares	Long
	Performance Appreciation Rights ("PARs")	Cash payment calculated as some measure of growth in corporate returns after the grant date. Can be settled in shares	Long
	Restricted Share Units ("RSUs")	Once vested, right to receive a cash payment equal to the value of a specified number of units, with unit value tracking share price	Mid
	Performance Share Units ("PSUs")	RSUs with performance-based rather than time-based vesting	Mid
	Deferred Share Units ("DSUs")	Right to receive a cash payment upon termination of employment, retirement or death equal to the value of a specified number of units, with unit value tracking share price	Long
Real Equity	Share Purchase Plan	Program to facilitate employee share purchase for FMV or at a discount	Mid/Long
	Restricted Stock	Shares that do not vest/cannot be sold until a restriction period lapses	Mid/Long
	Stock Options	Right to purchase a share upon payment of the exercise price. Can be settled in cash but favourable tax treatment may be lost	Mid/Long

share units (RSUs) or phantom share units (PSUs) – the value of which fluctuates with share price. Once phantom shares are vested, shareholders receive a cash payment equal to the value of an equivalent number of shares. Unlike options, phantom shares have both upside and downside for the holder. To avoid being taxed at grant, phantom shares typically vest within three years. PSUs feature performance-based vesting conditions to enhance their incentive capacity. U.S. employers should ensure grants of phantom shares to Canadian employees respect the three-year deferral limit.

Other forms of notional equity plans – deferred share units (DSUs), stock appreciation rights (SARs) and performance appreciation rights (PARs) – are not limited by the three-year deferral limit and can therefore provide longer-term incentives. DSUs are akin to phantom shares that do not pay out until termination of employment, retirement or death. Although DSUs permit longer-term deferral, DSU holders may have an incentive to terminate to take advantage of a spike in share price, depending on the plan design. This issue should be carefully considered at the plan design stage. SARs/PARs plans provide payments tied to growth in share price or earnings, but are vulnerable to the alignment-related criticisms noted above in relation to stock options.

"PLAIN VANILLA" CASH BONUS

Where simplicity is paramount, cash bonuses can of course be paid immediately, or deferred for up to three years, without any linkage to share price or performance.

The pros and cons of cash, notional equity and real equity should be weighed to ensure proper alignment of individual and organizational objectives in the short, medium and long term. Setting out plan terms in a formal document can prevent costly entitlement disputes and limit continued vesting/exercisability during a severance period. The text should clearly set out the treatment of incentive awards in the event of resignation, termination with or without cause, retirement, disability or death. And increasingly, employers are adopting plan language that permits clawback in the event wrongdoing is discovered after a grant. Careful drafting is critical to addressing these and other employment considerations, avoiding entitlement disputes and ensuring compliance with tax and securities laws.

John Prezioso is a partner in Hicks Morley's Toronto office, practising exclusively in the area of pensions, employee benefits and executive compensation. John advises a range of private and public sector clients on matters relating to pension plan governance, compliance and administration, including issues relating to benefit entitlement, communications, pension investment, conversions and wind ups. He also advises employers with respect to the administration and modification of group benefit plans, including retiree benefit plans. John regularly drafts and provides employment and tax advice in relation to equity-based and other incentive compensation plans.

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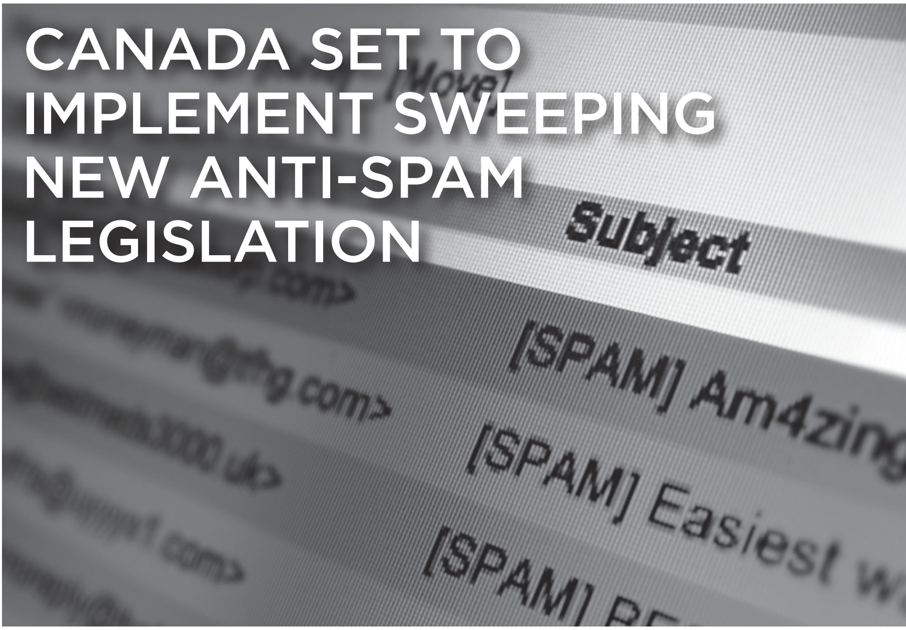
CANADA SET TO IMPLEMENT SWEEPING NEW ANTI-SPAM LEGISLATION



Canada is finally set to implement measures to reduce the prevalence of unwanted and often disruptive electronic communications, commonly referred to as “spam”. The measures are contained in “Canada’s Anti-Spam Legislation” (“CASL”) and regulations that are being made under it.

BY: JOSEPH COHEN-LYONS AND PAUL BROAD

Companies conducting business in Canada will be most interested in CASL’s anti-spam provisions, which severely restrict a company’s ability to use electronic communications as a means of conducting business.

The anti-spam requirements of CASL apply broadly and capture communications that are not traditionally understood as spam. In particular, CASL applies to all “commercial electronic messages” (“CEMs”), which are broadly defined in the legislation as any message that “it would be reasonable to conclude has as its purpose, or one or more of its purposes, to encourage participation in commercial activities.”

CASL aims to tackle spam by prohibiting a person from sending a CEM unless two requirements are met:

- the message conforms to certain specified criteria related to content and form; and
- the person sending the CEM first obtains the consent of the recipient, whether express or implied.

CASL contains a number of limited exemptions to the anti-spam protections set out above, some of which may be useful for businesses conducting electronic commerce. For CEMs that do not fall within one of the exemptions set out in CASL or its regulations, businesses will be required to obtain the recipient's consent and include certain information before being permitted to send the recipient a CEM.

THE CONSENT REQUIREMENT

CASL employs an "opt-in" model to consent that is significantly different from the "opt-out" model utilized in the anti-spam legislation in most other western countries, including the United States. Under the "opt-out" model, an organization can send CEMs until the recipient expresses a desire not to receive the CEMs. Under CASL, on the other hand, an organization must first obtain consent before it can send a CEM. Notably, a message sent for the purposes of obtaining consent is itself considered a CEM under CASL and, therefore, may not be sent without the consent of the recipient.

While consent may be implied or not required in some limited circumstances – for example, CASL allows for implied consent within existing business relationships where there has been commercial activity within the previous two years – express consent will generally be required before a CEM may be sent. The sender of a CEM has the onus of demonstrating the existence of a valid consent under CASL, which may be given in oral or written form. It is therefore important that companies carefully document the consents they receive.

THE CONTENT REQUIREMENT

In addition to requiring consent, CASL also requires certain information to be included in a CEM itself, including the name and address of the company (or person) sending the message as well as information enabling the person to whom the message is sent to readily contact the sender. All CEMs must also clearly and prominently set out an unsubscribe mechanism that allows recipients to "readily perform" the unsubscribe function.

ENFORCEMENT

The anti-spam provisions of CASL will be enforced by the Canadian Radio-Television and Telecommunications Commission ("CRTC"), which is given broad powers under the statute to investigate allegations of misconduct and impose penalties to enforce non-compliance. CASL provides for severe penalties for non-compliance, with the maximum penalty per violation set at $1 million for an individual and $10 million for a corporation.

CASL also creates a unique private cause of action available to persons who allege a violation of the Act. This means that a person can rely on an unsolicited CEM as the foundation for a civil action and raises the risk of class actions being initiated under CASL.

PREPARING FOR CASL

CASL has yet to be proclaimed into force. Currently, the federal Department of Industry is finalizing regulations that will clarify some of the requirements under CASL. It is expected that the regulations will be finalized sometime in the next 6 to 12 months, with CASL being proclaimed into force shortly afterward. Thus, CASL is unlikely to be implemented until at least sometime in the autumn of 2013. Nevertheless, it is essential that organizations begin to prepare for its implementation now.

Once implemented, CASL will provide a three-year transitional period during which time organizations will have deemed implied consent to send CEMs to any person with whom they have an existing business or non-business relationship that includes the sending of CEMs. This deemed implied consent will provide organizations with a useful time frame during which they should seek to obtain express consent.

Even with the transition period, organizations and business should take the following steps as soon as possible to ensure compliance with CASL:

- review marketing, advertising and external communication practices to determine to what extent they involve CEMs that are caught by CASL;
- consider whether consent can be implied based on an existing business or non-business relationship;
- develop a process by which existing business and non-business relationships can be recorded and tracked with reference to the two-year time frame used by CASL to define such relationships;
- develop a means for obtaining and appropriately recording express consents;
- develop a system to reliably record express consents and to track any changes to consents that have been obtained;
- develop a policy and processes to ensure that all CEMs contain the prescribed information, including the required unsubscribe mechanism; and
- ensure processes are in place to respond to unsubscribe requests in a timely manner.

Businesses that take these steps now will be better positioned on the long road to CASL compliance.

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May 15	Information and Privacy Roundtable for In-House Counsel
June 5	Unjust Dismissal Complaints: Being Prepared from Start to Finish
September 11	Risk Management
October 9	Negotiations and Bargaining
October 23	Disability and Employment
October 30	To Be Determined
November 13	Human Rights
November 20	To Be Determined

**Accreditation pending, visit hicksmorley.com/advantage for details*

HR QUICK HITS

Federal and proposed Ontario legislation will give employees child-related leaves

The recently enacted federal *Helping Families in Need Act* will soon permit employees to take job-protected leaves under the *Canada Labour Code* to care for a critically ill or injured child, or where a child has disappeared or died as the result of a suspected crime. Similar legislation has now been tabled in Ontario. If passed, Bill 21, *Employment Standards Amendment Act (Leaves to Help Families), 2013* will allow eligible employees to take unpaid leaves of absence to care for a critically ill child or where it is probable that a child's death or disappearance is the result of a crime. Bill 21 would also provide for family caregiver leaves, a new leave to care for relatives with a serious medical condition.

OTTAWA'S PENSION PRESENCE

Lisa Mills joined Hicks Morley in 1998 in the early days of the firm's pension and benefits law practice area. Fast forward 15 years and she's now part of a 12-lawyer group that remains solely focused on client pension, benefits and executive compensation issues. We spoke to Lisa in March about her career, her move to the Ottawa office and the big trends in pensions.

Had you always had your sights on being a lawyer?

No. Unlike many lawyers in the firm, it wasn't a childhood dream for me. In the last year of my Commerce degree at McMaster, I took a business law course and loved it. I thought I could somehow marry my interest in finance and tax with the law but wasn't sure where that would take me. I decided to go to U of T for law school.

What led you to the pensions area?

There's a great legal clinic at U of T – the Advocates for Injured Workers. Law students work with workers' compensation claimants. I enjoyed my work there and ended up as a clinic co-director. I learned to really listen to clients and liked having the chance to argue some appeals. My math and finance background was put to good use as it happened that the more significant cases I took on involved earnings calculations and requests to commute disability pensions. I also discovered that I enjoyed employment and labour law.

I articled at a firm with a strong labour and pensions practice and realized quickly that pensions would be a good choice given my background. After I was called to the Bar in 1997, I started my legal career at a pension consulting firm where I learned about pensions from the ground up, working with the actuaries and other consultants.

What prompted your move to Hicks Morley?

I was looking for more client contact and I missed having the chance to be on the front line dealing with broader legal issues relating to pensions and benefits. I also wanted the chance to do some litigation. I met Elizabeth Brown, who heads our practice group, at a conference in 1998. Hicks was growing its practice so the timing was right.

What was it like for you when you first arrived?

It was a great time to start. There weren't many of us in the group, and I was lucky enough to have a hand in most of the significant pension files at the firm. At that time, we were still doing a lot of surplus ownership opinions and refund applications. We were dealing with government downloading initiatives that resulted in significant pension issues, and we were also starting to see challenges to retiree benefits changes in the form of class proceedings.

How has your work at the firm changed over the years?

The work has changed a lot. We're not dealing with surpluses anymore. I have been counsel on a number of insolvency matters, and have developed expertise with one plan design aimed at addressing pension risk – the jointly sponsored pension plan model.

Every time you open a newspaper, it contains a pension or benefit article. The cost and risk of sponsoring a pension plan have a more significant profile now. At the beginning of my career, my main client contacts were in human resources. Now, it is much more common to be reporting into finance professionals as well. Plan design, funding and investment are increasingly recognized as being intertwined and clients are now adopting a more multi-disciplinary approach to managing pension risk.

Every time you open a newspaper, it contains a pension or benefit article. The cost and risk of sponsoring a pension plan have a more significant profile now.

How has your role at the firm changed?

I am now significantly involved in business and strategic planning for the Pension, Benefits and Executive Compensation Practice Group and in marketing our services to clients. But the biggest change was my move to Ottawa at the end of 2002. I was working in Toronto and my husband-to-be was working in Ottawa. Luckily we had just opened an Ottawa office and the firm agreed to the move. There are now seven lawyers in our Ottawa office. I have the best of both worlds – I work out of a small collegial office with all the benefits of being part of a 12-person practice group within a 100+ lawyer firm.

My move to Ottawa also opened up other opportunities, like developing and teaching a pension law course at Queen's University – the first of its kind there. I really enjoy the teaching role. More law students are seeing that pensions is an important area of study whether they end up in corporate law, family law, or in a labour and employment practice.

I recently co-authored the Public Pensions title for the *Canadian Encyclopedic Digest* with one of our associates, Susie Taing. It addresses CPP, Old Age Security, and provincial supplements made available to seniors. It's important not to lose sight of the fact that private pensions supplement government-sponsored programs and that changes to those programs will impact private arrangements.

Any trends for the future? What do clients have to watch for?

Clients are looking at alternatives to the traditional single-employer DB plan whether through different cost-sharing and risk-sharing arrangements – including joint sponsorship or target benefit arrangements.

On the DC side, I expect challenges relating to the current levels of financial literacy of DC participants. There hasn't been a great deal of regulation of DC plans and our advice has been based on fiduciary duty and negligent misrepresentation risks but I see a trend toward more regulatory guidance as DC plans gain prominence as the primary pension design used in the private sector. Education and communication of the target retirement income to be produced by DC plans are likely to feature in future regulations.

For employee benefits the main trends are continued cost containment by maintaining control over benefit promises and making changes. I would watch for more pressure to pre-fund benefits and protect long-term disability claimants affected by corporate insolvencies.

Governance issues will also continue to gain importance in shaping the administration of pension plans. Pension reform continues to make compliance reviews a key element of ongoing plan governance.

Clients are looking at alternatives to the traditional single-employer DB plan whether through different cost-sharing and risk-sharing arrangements – including joint sponsorship or target benefit arrangements.

How about your spare time – when you aren't thinking of retirement issues?

We live in Manotick, Ontario, just outside of Ottawa and have a young family, so it's very much kid-focused. We have two children, Zachary and Madeline.

I've had a reduced hours arrangement since Zachary was born and we learned that he has Down Syndrome. The firm has been unbelievable in the support I've received. I've been able to make sure we are meeting Zach's special developmental needs while still being fully involved with the firm as a partner and practising lawyer. I have to work hard at both ends to make it work, but the support is there for me to do it. That says a lot about the firm – it's really given me a life I love both inside and outside of the office.


PENSION? PLAN.
With 12 lawyers devoting 100% of their practice to pension, benefits and executive compensation issues, Hicks Morley is at the forefront of solutions and innovations in these areas. And our expertise is backed by the unparalleled litigation, labour relations and negotiations resources of Canada's leading human resources law firm. Find out more at hicksmorley.com
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