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Update

Pension Law

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Proposed Changes to Federal Pension Laws Announced

Yesterday, the Honourable Jim Flaherty announced proposed changes to federal pension laws. The majority of the changes will only affect registered pension plans that cover employees who fall within the federal government's jurisdiction (including employees of airlines, railways, radio broadcasters, banks, ferries and shiplines). However, there is a proposed increase to the pension surplus threshold under federal tax legislation that would impact all pension plans, including those registered in Ontario. In addition, there is a proposed change to the federal investment rules which could prompt provincial changes, as Ontario's pension investment rules (as well as the pension rules in several other provinces) currently refer to the existing federal investment rules.

Proposed Change to Tax Surplus Limit

Canadian tax laws restrict the amount of surplus that a defined benefit pension plan is allowed to hold. Once a pension plan reaches the maximum level of surplus allowed under the tax laws, employer contributions to the plan must generally be suspended until the plan's funded level drops to an acceptable level.

The announcement proposed that the current surplus threshold of 10% be increased to 25% and that this increase apply in respect of employer contributions relating to current service costs for 2010 and subsequent years. This change would allow pension plans to potentially build more of a funding buffer in the pension fund during good times, with the aim of minimizing the adverse effects experienced by pension plans during economic downturns.

Proposed Changes to Pension Investment Rules

The announcement indicated that the pension investment framework would be modernized and certain changes would be made. The quantitative limits restricting pension plan investments in respect of resource and real property investments would be removed, but pension plans would be prohibited from making any investments in the sponsoring employer's own debt or shares. In addition, the current restriction prohibiting a plan from investing more than 10% of its assets in any one entity would be amended to be based on a market value test of the assets of the plan (as opposed to the book value).

Notably, the proposed changes do not include the removal of the so-called "30% rule", which restricts pension plans from investing plan monies "in the securities of a corporation to which are attached more than 30 per cent of the votes that may be cast to elect the directors of the corporation". This rule has been criticized for being antiquated and not in touch with current business realities.

The current Ontario regulations incorporate the existing federal regulations. Accordingly, if these proposed changes are implemented federally, and if Ontario wishes them to apply to pension plans registered in the province, Ontario would also be required to amend its regulations.

Other Proposed Changes That would Affect Federally Registered Plans Only

The announcement indicated significant proposed changes that would affect only federally registered pension plans, which include:

- Requiring pension benefits to be fully funded in the event that a pension plan is terminated.
- Eliminating sponsor declared partial terminations.
- Allowing employers to take contribution holidays only where a pension plan is more than fully funded by a solvency margin of 5% of solvency liabilities. Plans in surplus would also be required to file valuations on an annual basis to ensure that any contribution holidays taken are based on a recent determination of the plan's funded status.
- Restricting employers from amending a pension plan to provide benefit enhancements where the pension plan is significantly under funded or would be following the amendment.
- Enhancing certain member disclosure requirements in respect of the pension plan.
- Changing the vesting period from 2 years to immediate vesting of pension benefits for plan participants.
- Adding rules that will apply specifically to defined contribution pension plans. These rules will provide guidance on the responsibilities of the various stakeholders and will take into account the Guidelines for Capital Accumulation Plans released by the Canadian Association of Pension Supervisory Authorities. They will also eliminate the requirement for such plans to have a Statement of Investment Policies and Procedures.
- Adding rules that may help facilitate dealing with plan specific near-term funding issues. These rules would allow plan specific funding arrangements to be negotiated in respect of distressed pension plans.

Draft legislation in respect of these proposed changes has not been provided at this time and no guidance has been given as to when such draft legislation may be available.

If you have any questions regarding these proposed changes and how they may affect you, please feel free to contact any member of our Pensions, Benefits and Compensation Group:

Maureen Berry
mberry@goodmans.ca 416.597.4287

Patricia Robinson
probinson@goodmans.ca 416.597.4144

Susan Rowland
srowland@goodmans.ca 416.597.4277

Gale Rubenstein
grubenstein@goodmans.ca 416.597.4148

Candy Schaffel
cschaffel@goodmans.ca 416.597.4153

Jana Steele
jsteele@goodmans.ca 416.597.6274