Group Savings & Retirement

Legislation matters

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Proposed Temporary Solvency Funding Relief Measures – Quebec is showing the way!

This year, several defined benefit (DB) pension plans will be required to file their actuarial valuation as at December 31, 2008.

A certain number of jurisdictions have already announced temporary solvency funding relief to DB pension plan sponsors, because of the poor stock market performance in 2008.

Quebec

In November 2008, Quebec had set up a committee with representatives from employers (the *Conseil du patronat du Québec* and the *Fédération des chambres de commerce du Québec*), unions (CSN and FTQ), the *Régie des rentes du Québec*, and the Ministry of Employment and Social Solidarity, so they could make recommendations to the Quebec government.

In December 2008, the Quebec government announced temporary relief measures for DB pension plan sponsors based on the committee's recommendations. Thereafter, on January 15, 2009, Quebec adopted Bill 1, *An Act to amend the Supplemental Pension Plans Act and other legislative provisions in order to reduce the effects of the financial crisis on plans covered by the Act.*

Bill 1 provides the following measures:

- Retroactive application – i.e., as at December 31, 2008 – of the Revised Standard of Practice for Pension Commuted Values of the Canadian Institute of Actuaries. The new Standard is effective April 1, 2009. This could mean lower solvency deficiencies for valuations effective on or after December 31, 2008.
- Measures for retirees and members who are eligible to retire and are affected by plan wind-ups, if a bankrupt employer cannot cover a deficit.
  - The measures include allowing retirees to transfer the value of their reduced pension to a fund managed by the Régie des rentes du Québec when their plan's assets are insufficient to pay full benefits, in the hope of benefiting from future investment gains. Currently pensions for these retirees must be purchased from an insurer.
  - The Régie would administer the fund for up to 5 years and would then be required to purchase an annuity guaranteed by an insurer that is increased to offset the impact of the temporary solvency relief measures.
  - The government would fund the pension increase, unless the Régie manages to generate sufficient returns over those 5 years.
  - If the solvency ratio of the plan is at 70%, for example, but it would have been at 75% if the bankrupt employer had not used the temporary solvency relief measures, then the government would fund the remaining 5% at the time of purchase of the insured annuity, unless the Régie manages to generate sufficient returns over those 5 years.
  - If the bankrupt employer had not used the temporary solvency relief measures, the Régie would pay the pension benefits in accordance with the real solvency ratio of the plan.

- The date of plan wind-up or withdrawal of a participating employer must be after December 30, 2008 but before January 1, 2012.
- The Caisse de dépôt et placement du Québec will manage the investments for the fund.
- A draft regulation is expected to be released for comments in early April. The regulation will provide, among other things, the investment policy.

In addition, it is expected that another draft regulation would be released in early April for comments to introduce the other temporary relief measures announced in December. A committee of experts has been set up in March with lawyers and actuaries to help the *Régie* in the drafting of this regulation. These measures are the following:

1. Consolidation of solvency deficiencies as at December 31, 2008 in order to put all deficits together and therefore, this would translate into a lower global contribution required from the employer.
2. Extension of the period of amortization regarding the solvency payments from 5 years to 10 years when DB pension plans have a solvency deficit. However, the resulting amortization payment could not be lower than the amortization payments that would have been required without the occurrence of the financial crisis.
3. Smoothing of assets over five years, which would increase the assets as at the actuarial valuation date and therefore, reduce the pension plan deficit.

These new proposed measures would only apply for years 2009, 2010 and 2011.

To take advantage of these new measures, DB pension plan sponsors would have to immediately apply the funding rules provided under Bill 30, which would normally come into force on January 1, 2010 – i.e., the obligation to file an annual actuarial valuation, instead of triennial valuations, and the obligation to pay a special contribution, in one lump sum payment, if a modification to the plan has the effect of lowering the solvency ratio below 90%.

Another committee has been set up to look at difficult issues for pension plans sponsored by municipalities, universities and daycare centers, since these plans have been subject to different funding rules since 2007. A draft regulation is expected to be released in May for further commentary.

Federal

The federal Minister of Finance, Jim Flaherty, proposed in his Economic and Fiscal Statement of last November, "to allow plans to extend their solvency deficiencies as at December 31, 2008, subject to certain conditions. In particular, both members and retirees would need to agree to the extended schedule, or the difference between the 5- and 10-year payment schedules would need to be secured by a letter of credit. One of these two conditions would need to be met by December 31, 2009. If buy-in by plan members or a letter of credit were not secured by the end of 2009, the plan would be required to fund the deficiency over the following 5 years."

As indicated in our special edition of *Legislation matters* on the 2009 Federal budget, further pension funding flexibility will be provided by increasing the 110% limit on asset value smoothing.

In a letter dated March 6, 2009 to actuaries of federally regulated DB pension plans, the Office of Superintendent of Financial Institutions (OSFI) has specified rules on asset smoothing for solvency valuations. Smoothing of assets up to 110% of market value is permitted in actuarial reports with effective dates of November 1, 2008 or later. For actuarial reports that are prepared in accordance with the solvency funding relief regulations announced in last November, smoothing of assets up to 115% of market value is permitted on a temporary basis only; the solvency funding relief regulations have not yet been issued. An instruction guide with more details on asset smoothing for solvency valuation rules is targeted for release in early April.

Finally, last December, OSFI issued a note allowing federally registered DB pension plans to apply the Revised Standard of Practice for Pension Commuted Values of the Canadian Institute of Actuaries for valuations at effective dates on or after December 12, 2008 as long as the report is submitted on or after April 1, 2009 and the plan is not terminated before that date.

Ontario

The Ontario government also announced solvency funding measures last December that would allow DB pension plans to extend new solvency amortization periods from 5 to 10 years. Access to solvency extensions for plans that are not jointly governed would be tied to the consent of active members or their collective bargaining agents and retired plan members.

Amendments to the regulation under the *Pension Benefits Act* will be required to introduce these new measures.

Ontario has announced that it will allow early implementation of the Revised Standard of Practice for Pension Commuted Values of the Canadian Institute of Actuaries for solvency valuations.

Finally, on March 26, 2009, Ontario Minister of Finance, Mr. Dwight Duncan, tabled the 2009 Ontario Budget, which is providing additional details on the solvency funding measures announced last December. It is proposed that these measures would apply to the next valuation filed on or after September 30, 2008.

Other Jurisdictions

Similar temporary funding relief measures are also applicable in other jurisdictions – i.e., Manitoba, Alberta, New Brunswick, Nova Scotia and Newfoundland and Labrador.

British Columbia has issued in January 2009 a note entitled *Guidelines for Requests for Solvency Extensions for Defined Benefit Pension Plans* that provides guidance to plan administrators who are considering making solvency extension requests.

Alberta and Saskatchewan have issued discussion papers proposing similar temporary funding relief measures. Comments had to be submitted by January 31, 2009. Alberta has amended since then the *Employment Pension Plans Regulation* to provide temporary funding relief for DB pension plans as a result of the decline in the funded and solvency position of Alberta registered DB pension plans following the world-wide investment losses of 2008.

2 The Jeffrey Mine Case – Class Actions will finally be heard in 2010!

The Superior Court of Quebec will start hearing in September 2010 class actions involving the *Régime de retraite des employés salariés de Mine Jeffrey inc.* (the pension plan for non- unionized employees) and the *Régime de retraite des employés horaires de Mine Jeffrey inc.* (the pension plan for unionized employees). Both pension plans are defined benefit pension plans.

The Court will have to determine as to whether the investment policy for both pension plans was prudent, according to the specific circumstances of this case.

This case is very important and will certainly set a precedent, because the whole issue of the plan administrator's fiduciary responsibility and of the third parties' responsibility is raised and will be argued in court. In other words, this case will hopefully clarify who is responsible for what.

We will keep you posted when the Superior Court of Quebec's decision is released.

Reminder

The proportion of investments in stocks in the pension funds have varied, between December 1998 and January 2003, to 73% from 44.7% due to investment policy changes during that period.

During that period, the company was going through very difficult financial times for several reasons and finally, it applied for the protection offered under the *Companies' Creditors Arrangements Act* in October 2002.

As of October 2002, the company ceased to pay contributions related to pension funds' liabilities, and it ceased to pay contributions related to current service as of February 8, 2003.

As a result, the *Régie des rentes* du Québec declared both pension plans wound up as at February 8, 2003.

On June 28, 2003, members of pension committees resigned and thereafter, the *Régie* decided to place the pension plans under provisional administration. In other words, the *Régie* became the provisional administrator for both pension plans.

The end result is a solvency ratio of 63.43% and therefore, that situation translates for former members into a loss of 36.57%. For example, if a former member was receiving or was expecting to receive an annual pension of $10,000, he would receive only $6,343 per year.

Now, the plaintiffs – i.e., the former members of both pension plans – are essentially requesting from both pension committees and their members, the consultant (the actuarial firm) and the investment manager an amount of $6,994,782 (with interest and the additional indemnity provided under the *Quebec Civil Code*) regarding the non-unionized employees pension plan, and an amount of $ 6,804,075 (with interest and the additional indemnity provided under the *Quebec Civil Code*) regarding the unionized employees pension plan.

Alternatively, the plaintiffs are requesting the consultant and the investment manager to pay to each former member on a pro-rata basis a portion of the above-mentioned amounts (with interest and the additional indemnity provided under the *Quebec Civil Code*), due to their extra-contractual fault.

3 TFSA – What happens in case of death?

The rules governing tax-free savings accounts (TFSA) are generally easy to understand.

However, when a TFSA holder dies, it's a different kettle of fish.

TFSA under an annuity contract (i.e., an insurance contract)

There is a deemed disposition of the contract immediately before the date of death. In other words, this means that when a holder dies, his TFSA becomes a non-registered plan, and all earnings that accrue under the TFSA after the holder's death will be taxable to the beneficiary.

All type of earnings that accrue after the holder's death must be reported as such (i.e., interest, capital gains, dividends, etc.). They cannot be reported as ''other income''.

The surviving spouse has the option of transferring the deceased holder's TFSA into his own TFSA, without affecting his TFSA contribution room limit. There is no time limit to do so. However, the surviving spouse will be taxed on earnings that accrue after the holder's death until he transfers the holder's TFSA into his own TFSA.

TFSA under a trust

The TFSA is deemed to continue to be a TFSA until the end of the year following the year in which the holder dies or when the trust ceases to exist, if earlier (this is called the ''exempt period''). The main effect of this deemed rule is that the trust continues to maintain its tax-exempt status during this period.

All income earned during the exempt period (i.e., accrued after the holder's death) and paid to the beneficiary, including a surviving spouse, is required to be included in the beneficiary's income. This payment will have to be reported on a T4A as "other income".

If the TFSA still exists after the exempt period, the trust will be taxable from that point on and will be treated as having disposed of, and reacquired, its property for its fair market value at that time. The trustee will be required to file a T3 Trust Income Tax Return and Information Slip for every year beyond the exempt period that the estate remains unsettled.

The surviving spouse has the option of ''transferring'' the holder's TFSA into his own TFSA. In fact, the surviving spouse may contribute payments made within the exempt period from a deceased spouses' TFSA into his own TFSA without affecting his unused TFSA contribution room limit. Such surviving spouse payments become an exempt contribution.

In order for the surviving spouse to designate an exempt contribution, the surviving spouse must designate their survivor payments as an exempt contribution on Form RC240, *Designating an Exempt Contribution to a Survivor Tax-Free Savings Account (TFSA)* within 30 days after the day on which the contribution is made.

An exempt contribution cannot exceed the payment received during the exempt period and the fair market value of the holder's TFSA at the time of death.

Note: If the deceased had named his spouse as his ''successor holder'', instead of his designated beneficiary, the TFSA will continue and the surviving spouse becomes the successor holder under the TFSA.

You can contact us

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legislation.matters@standardlife.ca

www.standardlife.ca

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Standard Life Assurance Limited

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