Legislation matters

October 2009

1 Kerry decision – A sound decision for pension plans

In the April 2008 issue of *Legislation matters*, we summarized the Ontario Court of Appeal decision, which dealt with, amongst other things, the use of surplus from a defined benefit (DB) component to fund a defined contribution (DC) component and with the payment of plan expenses from the pension plan trust fund.

We also indicated that the Supreme Court of Canada decided to hear the Kerry appeal on those issues, and that we would update you following the release of the Supreme Court decision.

The Supreme Court of Canada heard the Kerry appeal in November 2008 and released its judgment on August 7, 2009.

The majority of the Supreme Court of Canada dismissed the appeal and upheld the Ontario Court of Appeal decision. In fact, only two judges were dissident, and even then, only on the issue of the use of surplus from a DB component to fund a DC component.

The Kerry appeal essentially raised the following issues:

1. Whether the employer could use actuarially determined surplus pension funds to satisfy its contribution obligations in respect of both DB and DC components of the pension plan.
2. Whether the employer was responsible for paying plan expenses or whether such expenses were properly payable from the pension trust fund.

In brief, the Supreme Court of Canada concluded the following:

1. Surplus

a) ***Use of surplus from DB component to fund DC component*** – As long as the DC members are designated as DB trust fund beneficiaries and the plan documents allow it, then it is permissible for the employer to use the surplus under the DB component to fund its contribution requirements under the DC component of the plan. The majority of the Court concluded that no regulations were preventing the employer to retroactively amend the plan documents in order to designate DC members as beneficiaries of the DB trust fund, and no regulations were preventing a single plan and trust or the taking of DC contribution holidays. Interestingly, the majority of the Court found that "Retroactively amending the Plan takes no vested property right away from the DB members".

b) ***DB contribution holidays*** – The Court concluded that the employer was allowed, in this case, to take DB contribution holidays, regardless of whether the plan document wording expressly provide that the employer funding obligations are determined by actuarial calculations. This last remark from the Court clarifies the Court's findings in 1994 in *Schmidt v. Air Products Canada Ltd.*, where the Court concluded that an employer is allowed to take a contribution holiday as long as the plan document wording expressly provide that the employer funding obligations are determined by actuarial calculations, unless other plan wording or legislation prohibits it.

2. Payment of plan expenses – Based on the broad power of amendment and in light of prior plan documents such as the pension plan text and the trust agreement, both of which were silent on plan expenses, the Court concluded that the employer was allowed to pay plan expenses from the pension trust fund, even though the employer paid them previously. Again, it is interesting to note that the Court clarified that "[so] long as nothing in the plan texts requires the paying of expenses by the employer, funds in the pension trust can be used to pay reasonable and *bona fide* expenses". Even though only third-party plan expenses were paid from the pension fund, the Court added that "... whether the services are provided by third parties or the employer itself is immaterial as long as the expenses charged are reasonable and the services necessary".

It is important to note that the decision of the Supreme Court of Canada is based on specific provisions of the Kerry pension plan text and trust agreement and therefore, you should review your pension plan documentation with your lawyers or consultants before applying the Kerry decision to your situation.

Summary of the facts

The Kerry pension plan for its employees started in 1954. The plan was solely a DB pension plan.

Until 1984, the employer paid the plan expenses directly. In 1985, following amendments to plan documents, third-party plan expenses for actuarial, investment management and audit services were paid from the pension fund (i.e., approximately $850,000 between 1985 and 2002).

In addition, starting in 1985, the employer took a contribution holiday from its funding obligations (i.e., approximately $1.5 million by 2001).

In 2000, the plan text was amended to introduce a DC component. The DB component continued for existing members, but was closed to new employees who would join the DC component. Existing members were offered to stay in the DB component or to convert to the DC component.

The DB component is held by a trust company and the DC component is held with an insurance company.

After having notified the members, the employer took contribution holidays under the DC component by using the surplus accumulated under the DB component to fund its contribution requirements under the DC component of the plan.

A committee of members of the pension committee and former employees objected to these practices and asked the Superintendent of the Financial Services Commission of Ontario (FSCO) to investigate alleged irregularities. Thereafter, legal proceedings started after the Superintendent issued Notices of proposal.

On June 5, 2007, the Ontario Court of Appeal released its judgment and concluded that the employer was allowed to use the surplus accumulated under the DB component to fund its contribution requirements under the DC component of the plan and to pay plan expenses from the pension trust fund, even though the employer paid them previously.

2 Updated rules for Ontario's Life Income Fund (LIF)

In our last edition of *Legislation matters*, we explained that the Ontario Minister of Finance, Mr. Dwight Duncan, proposed in his 2009 Ontario budget to enhance access to locked-in funds by increasing the unlocking permitted on the acquisition of a new LIF from 25% to 50%, effective January 1, 2010.

Since then, this proposal has been passed and the *Pension Benefits Act* Regulation has been amended accordingly.

The main changes are the following:

Changes that will come into effect on January 1, 2010

- Anyone who purchases a new LIF on or after January 1, 2010 will have a one-time opportunity to withdraw in cash or transfer to an RRSP or RRIF up to 50% of the total market value of the assets of the fund. They will have 60 days from the day the assets were transferred into their new LIF to make the withdrawal application.
- Owners who have purchased a new LIF between January 1, 2008 and January 1, 2010, will have a one-time opportunity, from January 1, 2010 to December 31, 2010, to withdraw in cash or transfer to an RRSP or RRIF an additional 25% of the total market value of the assets of the fund that were transferred into their new LIF before January 1, 2010.

Changes that will come into effect on January 1, 2011

- Owners of old LIFs (i.e., purchased before January 1, 2008) or Locked-In Retirement Income Funds (LRIFs), will have a one-time opportunity, from January 1, 2011 to April 30, 2012, to withdraw in cash or transfer to an RRSP or RRIF up to 50% of the total market value of the assets of the fund.
- The rules to determine the annual maximum withdrawal amount from an old LIF or an LRIF will become standardized based on the rules under a new LIF – i.e., the greater of the following: the amount determined as per usual under a LIF and the amount of investment earnings of the fund in the previous year.
- Owners of old LIFs and LRIFs will no be longer able to transfer assets back to a Locked-In Retirement Account (LIRA). The transfer options will be limited to a transfer to a new LIF or the purchase of an annuity.

Changes that will come into effect on May 1, 2012

- Owners of old LIFs and LRIFs will no longer be able to withdraw or transfer 50% of the assets in their account.

Our current Ontario LIF owners, both old and new, will be notified by the end of this year of these new changes and any changes that will affect their contracts.

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Manitoba – Proposed pension regulation changes

Manitoba's Office of the Superintendent has undertaken a complete review of the Pension Benefits Regulation in order to implement changes made to *The Pension Benefits Act* in 2005.

Last June, Manitoba's Office of Superintendent released proposed regulatory amendments and asked for stakeholders to provide their comments by August 15, 2009.

Significant changes proposed include:

- clarifying administrator responsibilities
- providing for the rights and obligations of the pension committee and its members
- expanding the disclosure requirements for plan members and other beneficiaries
- prescribing ancillary benefits
- providing for phased retirement
- providing for a one-time transfer from a pension plan, LIF or LRIF to a prescribed RRIF
- providing for lump-sums withdrawals by non-residents
- clarifying the requirements for lump sums on shortened life expectancy
- clarifying the requirements for division of pension benefits and pensions on the breakdown of a relationship
- clarifying the requirements for plan termination or winding up and predecessor and successor plans
- changing the administrative requirements for prescribed retirement savings and benefit plans
- changing the maximum withdrawal calculation for LIF

These proposed changes would constitute a reorganization of the Manitoba pension regulation in order to be more in line with the other pension regulations across Canada.

It is interesting to note that it is proposed that pension committees be the administrators of pension plans with 50 members or more. Pension plans with less than 50 members would continue to be administered by employers.

The proposal regarding pension committees would provide for rules very similar to those applicable to the pension committees of Quebec-registered pension plans, including the obligation to call all members and beneficiaries to annual meetings.

We will provide you with more details in a future edition of *Legislation matters* once the proposed regulatory amendments come into effect.

You can contact us

Your feedback is important to us. If you have any comments about our publication, or if you would like us to address a particular issue or subject in a subsequent edition, please feel free to drop us a line at the following address:

legislation.matters@standardlife.ca

www.standardlife.ca

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Standard Life Assurance Limited

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