Cassels

Canadian Pension and Retirement Plans

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As the Canadian economy has come to a near standstill, public equity markets have declined sharply and interest rates have dropped. This has caused sudden unanticipated and significant financial hardships for defined benefit (DB) and defined contribution (DC) registered pension plans, along with other common types of employer-sponsored retirement savings plans in Canada.

Here we provide a summary of some COVID-19-related issues our clients are experiencing, along with various preliminary recent Canadian federal and Ontario provincial government initiatives in the pension and retirement savings area. Many of the other Canadian provinces have announced similar measures.

Financial Hardship Withdrawals

Employees who have suddenly become unemployed, or underemployed, often seek to draw on their retirement savings. Under Canadian pension legislation, which applies to DB and DC registered pension plans, neither loans from pension plans to employees nor withdrawals are permitted. That is because of the statutory "locking-in" rules in Canadian pension legislation which prevent withdrawals of pension entitlements until reaching retirement age, and then requires benefits to be paid only in the form of a lifetime pension. Any changes to these locking-in rules would require amendments to the legislation, and so far no Canadian government has proposed such a change.

In Canada, former employees who transfer their pension entitlements into a locked-in retirement vehicle (typically on termination of employment) may apply to the applicable pension regulator for financial hardship withdrawals. The rules for these withdrawals vary by jurisdiction.

A common alternative to a DC pension plan is a Group RRSP arrangement, often coupled with a deferred profit sharing plan (DPSP). In this type of arrangement, employee contributions (whether required or voluntary) are paid into the Group RRSP and employer contributions are paid into the DPSP. Since Group RRSP and DPSP arrangements are exempted from pension minimum standards legislation, they are not subject to the "locking-in" rules described above. Amounts can be withdrawn from these plans, subject to the contractual terms of the arrangement, and subject to income tax (but no other special tax penalty).

Some have called on the Canadian government to amend federal tax legislation to permit hardship withdrawals from Group RRSPs and other tax-assisted retirement savings vehicles on a more favourable basis (i.e., some form of tax holiday). So far, the government has not shown any willingness to consider such proposals.

Typically, DPSP arrangements do not contemplate employee or employer withdrawals during employment, because the contributions and investment income thereon are intended for retirement savings. Group RRSPs often permit employees to withdraw their own contributions while still employed, but usually impose some form of contractual penalty (i.e., in addition to the income tax payable at marginal rates on RRSP withdrawals), such as a cessation of employer matching contributions for some period after the withdrawal. Employers with Group RRSP and/or DPSP arrangements should review their plan documents and consider whether the current rules for such withdrawals remain appropriate. If the employer is considering reducing or suspending its own contributions, consideration should be given to reducing employee required Group RRSP contributions and perhaps also waiving any contractual penalties associated with employee withdrawals.

Reduction, Suspension or Cessation of Contributions

To conserve cash, many employers are seeking to reduce pension and retirement savings plan costs. In a Canadian DC pension plan, a reduction of ongoing contributions (whether by employer or employees) has always been permissible by plan amendment which does not require prior governmental approval. However, a plan amendment must be prepared and filed with the appropriate pension regulator and a notice complying with the "adverse amendment" rules in the applicable pension standards legislation must be sent to affected plan members.

Canadian registered pension plans are subject to two separate forms of statutory registration and regulation – under the federal *Income Tax Act,* and under the applicable minimum pension standards legislation which is provincial except in the case of federally regulated employees for whom the federal minimum pension standards legislation applies. Both the federal tax authority (the Canada Revenue Agency or CRA) and Ontario's pension regulator, the Financial Services Regulatory Agency (FSRA) have long published guidance requiring that employers make a minimum contribution of at least 1% of employees' earnings to a DC plan. However, both have recently informally indicated employers may temporarily suspend their DC plan contributions (i.e., reduce to zero), at least for the balance of 2020.

For Canadian DB plans, employer contributions are required per the most recently filed actuarial valuation report. A DB pension plan may be amended prospectively to reduce the future accrual of pension benefits, and a fresh actuarial valuation would have to be filed in order to reduce contributions to correspond with the reduction in benefit accrual. However, this would not relieve the employer from the requirement to continue making special payments to fund deficiencies not related to current service accrual.

Beginning in 2016, many Canadian provinces, including the two largest (Ontario and Quebec), amended their pension legislation to relieve DB plan sponsors from solvency funding requirements by moving to a going concern funding model with a buffer (in Ontario, called a "provision for adverse deviations"). The federal pension minimum standards legislation (applicable to federally regulated employers in the banking, telecommunications and inter-provincial transportation sectors) still requires pension solvency deficits be funded over five years.

So far, the Ontario government has not announced any changes to DB plan funding rules in connection with the COVID-19 pandemic.

On April 15, 2020, the federal government published a news release stating "We are providing immediate, temporary relief to sponsors of federally regulated, defined benefit pension plans . . . in the form of a moratorium, through the remainder of 2020, on solvency payment requirements for defined benefit plans . . . The government also recognises that the impacts of the global pandemic on pension plan assets and liabilities could also significantly affect solvency funding obligations in 2021. The government will consult with stakeholders over the coming months on options to provide relief from 2021 funding obligations, as necessary." This new moratorium is voluntary, so plan sponsors can elect whether or not to continue making solvency payments. Current service contributions are still required to federally regulated plans.

In 2009, during the last financial crisis, the federal government enacted its Solvency Funding Relief Regulations, which allowed employers to stretch out the amortization of solvency deficiencies from five years to ten, but required agreement of plan members first. These 2009 special federal Regulations expired in November 2019. The feds have also granted one-time funding relief measures to insolvent employers such as Canadian Press (2009) and Air Canada during its CCAA restructuring (2003-2004).

DB plan sponsors may wish to consider filing a fresh actuarial valuation at an earlier date then required by statute in order to defer recognition of adverse investment returns or increased actuarial liabilities due to lower discount rates.

Employers considering reduction of pension contributions should of course consider the applicable employee relations, employment contractual and collective bargaining issues before proceeding.

Commuted Value Transfers

Under Ontario pension law, terminated employees have "portability" rights, permitting them to elect to transfer out of their pension plan into a personal retirement account (or another pension plan) the commuted value of their accrued pension entitlement. In a DB pension plan, if the plan has a "transfer ratio" of 1.0 or greater, the commuted value may be transferred without regulatory approval. The transfer ratio is a prescribed measure of whether the pension plan has sufficient assets to meet all of its liabilities. If administrator knows or ought to know that the transfer ratio is less than one, and either has decreased by

10% or more from the most recently determined ratio, or has fallen below 0.9, the administrator must obtain FSRA approval before transferring the commuted value to a terminating employee. This rule is intended to help prevent terminated employees receiving a disproportionate share of the plan's assets, compared to the share of such assets in the plan remaining for current and former members. Due to declining transfer ratios in DB pension plans, FSRA has recently reminded plan administrators of their obligations under these rules. Many more DB plan administrators, and their terminated former employees, will be now affected by this rule.

For federally regulated pension plans, the Office of the Superintendent of Financial Institutions (OSFI) issued a directive implementing a temporary full freeze on portability transfers from DB pension plans, effective March 27, 2020. A similar freeze applies to annuity purchases of defined benefits. Death benefits payable to non-spouses and payments of additional voluntary contributions are excluded from the freeze. Note that neither of these restrictions on commuted value transfers apply to DC pension plans (or Group RRSPs or DPSPs which are exempt from pension standards legislation). Similarly, the freezes do not affect pensions that are already in pay.

Notices and Filings

For Ontario-registered pension plans, FSRA takes the position that it has discretion on some matters under its enabling legislation, but not on other matters. Where discretion exists, FSRA intends to exercise that discretion taking into consideration the evolving COBID-19 crisis. FSRA issued the following guidance in this area:

- The deadline for filing of required documents within prescribed timelines (such as annual reports, audited financial statements, actuarial valuations, etc.,) can be extended for 60 days upon request to FSRA (per existing legislation). FSRA will now consider requests for extensions beyond 60 days upon request.
- Annual statements, termination and retirement option forms, etc., must be provided to plan members and former members within prescribed time lines, but this may be difficult to do given workplace closures. FSRA invites dialogue about such issues with the pension officer assigned to the plan, and suggested penalties for non-compliance are unlikely.
- Applications to FSRA (such as pension asset transfers and wind up applications) will continue to be processed, but with some delay due to current disruptions. New applications should be submitted by email since most FSRA staff are working remotely.
- In 2018, FSRA and its predecessor FSCO was given a new power to impose monetary penalties (Administrative Monetary Penalties or AMPs) for contraventions of certain provisions under pension legislation and regulations, obviating the need for a Court hearing to impose such penalties. Individuals can be fined up to $10,000 and corporations up to $25,000 and such fines cannot be paid from the pension fund. FSRA has been slow to exercise this new power, but recently announced it had begun to impose these penalties for non-compliance. However, it seems likely FSRA will be

more reluctant to exercise this new power during the current COVID-19 crisis other than in exceptional circumstances.

For federally regulated pension plans, OSFI announced a three month extension for the deadlines to file Annual Information Returns, Financial Statements, Actuarial Reports and Information Summaries and annual member and former member statements. Instead of filing or transmitting these within 6 months of year end, plan administrators may now file and transmit these within 9 months of plan year end (with a caveat that plan members and former members should be advised of the delay in sending their annual member statements). These extended deadlines apply only to plans with year-ends occurring between September 30, 2019 and March 31, 2020.

Transition of Employment from Full to Part Time, and Leaves of Absence

Canadian minimum pension standards legislation typically provides that part time employees with sufficient hours of work are entitled to accrue pension benefits in any pension plan provided by the same employer for its full time employees. For example, in Ontario part time employees who earn at least 35% of YMPE or work at least 700 hours per year must be entitled to join a pension plan for full time employees after two years of service. Therefore many or most employees transitioning from full to part time employment will continue to accrue benefits in the pension plan.

For employees placed on COVID-19 related leave, Ontario (and most other provinces) have amended employment standards legislation to mandate that employees on leave related to COVID-19 (or other infectious diseases) continue to participate in employer sponsored benefit plans, including pension and other retirement savings plans even if the leave is unpaid (unless the employee elects in writing not to do so). Thus, employers are obliged to contribute to such plans in respect of such employees on leave, even if the leave is without pay and even if such employees do not make their own required contributions to such plans.

RRIF Withdrawals

Registered Retirement Income Funds are tax-exempt retirement savings vehicles for individuals who have reached retirement age and begin to receive distributions from their retirement savings. RRIFs are initially funded by tax-exempt transfers of lump sum amounts from registered pension plans, RRSPs and other similar tax-deferred retirement savings arrangements. Under Canada's Income Tax Act, there are minimum required distributions from RRIFs that apply once the holder reaches age 71. Because of declining market values of RRIF assets, this could force holders to sell securities held within the RRIF at depressed valuations.

To partly address this issue, the federal government has announced that required RRIF withdrawals will be reduced by 25% for 2020.
