PBSA Update

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PBSA Update is issued by the Private Pension Plans Division, Office of the Superintendent of Financial Institutions (OSFI). OSFI administers the *Pension Benefits Standards Act, 1985* (*PBSA*)

SPECIAL EDITION

This Special Edition of *PBSA Update* is intended to tell interested stakeholders about the new requirements of the recently amended PBSA and the significance of the new amendments for plan members, plan sponsors, consultants and others.

We include with this Special Edition of *PBSA Update*, a copy of Bill S-3, and explanations of the major amendments to the PBSA. Some of the changes, most notably distribution of surplus, information to members, and void amendments, require the support of Regulations, which are discussed in a separate article.

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1. Background to the PBSA Amendments

The *Pension Benefits Standards Act, 1985,* (PBSA) is administered by the Office of the Superintendent of Financial Institutions (OSFI), a federal government agency. Some 1,100 pension plans are registered under the PBSA. They cover about 500,000 members and have more than $50 billion in assets.

The PBSA and the *Office of the Superintendent of Financial Institutions Act* (OSFI Act) were recently amended by Bill S3 to meet the emerging challenges of private pension plans. The amendments to the OSFI Act extend OSFI's mandate and clarify its supervisory role in monitoring the financial condition of pension plans. The OSFI Act now recognizes that a reasonable balance must exist between the expectations of plan members and beneficiaries that obligations will be met and the role of the regulator in assessing whether such promises can be met and taking appropriate action when required.

Prior to this year, the PBSA had not been materially revised since coming into force in 1987. The supervisory and prudential systems in financial institution legislation were strengthened on three occasions during the past few years and OSFI believed that similar changes were required to the PBSA.

As well, some federally regulated pension plans have experienced financial pressure as a result of demographic and economic factors, including an aging workforce and corporate downsizing. OSFI realized that its supervisory framework did not include the flexibility, range of powers and regulatory tools needed to deal with plans where we had funding and/or compliance concerns. For example, before the recent amendments, the key power of the Superintendent was deregistration. This option was only available where a plan did not meet the standards for registration and was not necessarily in the best interest of the plan beneficiaries. Under the amended PBSA, the Superintendent will have the powers necessary to deal properly with plans in difficulty.

In July, 1996 the Government issued a White Paper entitled *Enhancing the Supervision of Pension Plans under the Pension Benefits Standards Act, 1985*. The paper was widely distributed and many stakeholders commented on the proposals. For the most part, the comments were supportive. All views were considered in developing the amendments which were introduced in the House of Commons as Bill C-85 in March, 1997.

Last fall, the government reintroduced the Bill, with minor changes, in the Senate as Bill S-3. The Bill was passed by both chambers and received Royal Assent on June 11. It is expected that an Order in Council will be issued by September declaring the effective date of the amendments. This is expected to be October 1, 1998 for all changes except for section 9.2, which is expected to become effective on April 1, 1999.

2. Explanation of Amendments

Registration of Pension Plan

Amended Sections of the PBSA	Item
10 (1) & (2)	As the superintendent no longer has a duty to examine each document before issuing Certificate of Registration, the administrator of a pension plan must ensure that the pension plan documents comply with the legislation before submitting them for registration. The administrator must also include with their Application for Registration a declaration that the plan complies with the Act and Regulations.

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Registration of Pension Plan

Amended Sections of the PBSA	Item
10 (3)	When the administrator has filed the appropriate documents and has declared that the plan complies with the legislation, the Superintendent may register a plan on receipt of the documents or refuse registration of the plan if it does not comply with the PBSA and Regulations notwithstanding a declaration of the administrator to the contrary.
10 (5)	This subsection requires the Superintendent notify the administrator of the particulars of non-compliance when he decides to refuse registration of a pension plan.
10 (6)	Every plan filed for registration must provide for the use of surplus on both a going concern and termination basis. This requirement will facilitate any distribution of surplus at a later date.

Disclosure

Amended Sections of the PBSA	Item
9.1 (1)	An administrator must now advise the holder or custodian of the pension fund of all amounts to be remitted to the fund and the expected date of the remittance.
9.1 (2)	The plan administrator and custodian are now required to notify OSFI if the employer is not remitting the required contributions to the fund.
28 (1)(b)(iii)	In the past, the PBSA required that the plan administrator include the funded ratio of the plan in the annual statement. As the funded ratio (assets over liabilities on a going-concern basis) was rather meaningless to a member, the Superintendent can now prescribe the ratio. The prescribed ratio will be the solvency ratio (assets over liabilities on a plan termination basis). This is more meaningful to members, particularly terminating ones who are entitled only to a transfer value of their pension benefit credit multiplied by one, where the solvency is one or above, or the actual solvency ratio, where the solvency ratio is less than one.
28 (1)(c)(i)	Former members and retirees will now have the same rights as members to review plan documents and financial statements filed with OSFI.

Void Amendments

Amended Sections of the PBSA	Item
10.1 (2)(b)	A plan amendment which would cause the solvency ratio of the plan to fall below the prescribed solvency ratio level will be void unless the amendment has been approved by the Superintendent.

Enhanced Powers for the Superintendent

Amended Sections of the PBSA	Item
11 (1) & (2)	This amendment permits the Superintendent to issue a direction of compliance (DOC) to a plan administrator, employer, or any person connected with a plan regarding conduct contrary to safe and sound financial or business practices, and for breaches of the terms of the plan or the PBSA.
12 (3.1)	The Superintendent may specify modifications to the actuarial practices of the CIA and the accounting principles of the CICA for purposes of financial reporting. This amendment gives the Superintendent the same powers found in other financial sector legislation.
29.1 (1)	The Superintendent may remove an administrator and appoint a replacement administrator where a plan has been terminated and the administrator is insolvent or unable to act; or if in the Superintendent's opinion, it is in the members' best interest to appoint a replacement administrator.
33.1	This section permits the Superintendent to apply to the Federal Court for an order requiring an administrator, employer or other person to cease a contravention or perform actions required under the PBSA or a DOC.
33.2 (1)	The Superintendent may initiate any action that could be initiated by a member, former member, or any other person entitled to a benefit or refund from the plan. This amendment allows the Superintendent to institute civil action and seek damages against any person for losses to the fund. Previously, a prosecution under the PBSA or the Criminal Code did not result in restitution to the fund.
34 (1) & (2)	These amendments clarify the Superintendent's ability to request information in any form that the Superintendent specifies and clarify that the duty to inspect plans does not include a formal "audit."
34 (3)	This subsection allows the Superintendent to obtain independent professional advice at the expense of a plan. For example, if an independent party is engaged to do an inspection, any expenses incurred in preparing the report may be charged to the plan.

Plan Governance

Amended Sections of the PBSA	Item
7.5 (1) & (2)	These subsections enable the Superintendent to require that a plan administrator hold a meeting and consider matters set out in writing by the Superintendent. The Superintendent may attend or be heard at the meeting and may require that those entitled to benefits be invited as well as interested parties such as accountants and actuaries.
8 (4.1)	This amendment incorporates the prudent portfolio approach to investment management as found in other financial institution legislation.
8 (5.1)	This subsection limits the liability of the plan administrator with respect to breach of standard of care if the plan administrator relied in good faith on professionals.

Surplus (Not effective until April 1, 1999)

Amended Sections of the PBSA	Item
2.1	The surplus is the amount, determined in the prescribed manner, by which the assets of a pension plan exceed liabilities. The definition is required because the legislation now provides for entitlement to surplus.
9.2 (1)	This permits the withdrawal of surplus if the employer can establish entitlement, if the requirements of the Regulations are met, and if the Superintendent approves such a withdrawal.
9.2 (2)	This subsection requires the Superintendent to recognize an employer's claim to all or part of the surplus established under Section 9.
9.2 (3) & (4)	These amendments establish an employer's entitlement to the surplus if more than two-thirds of members, former members, and other persons within a prescribed class consent to employer's proposal. If more than one half but less than two thirds of the persons in each category consent, the employer may submit the proposal to arbitration. If the plan is terminated, the employer has no option and must submit the matter to arbitration if more than half but fewer than two thirds vote in favour of the proposal.
9.2 (5)	Where a plan is being wound up or liquidated, and the employer has not established entitlement to all or part of the surplus, the employer's claim to the surplus shall be submitted to arbitration within eighteen months after the termination date, subject to an extension by the Superintendent.
9.2 (6)	If the proposal or claim to surplus is submitted to arbitration, all parties are deemed to have agreed that the arbitrator's decision is binding.
9.2 (7 to 15)	These subsections explain the arbitration process, which will be detailed in the amended Regulations.

Additional Items

Amended Sections of the PBSA	Item
6 (1)(a.1)	This paragraph authorizes the Minister, with the approval of the Governor in Council, to enter into an agreement with the appropriate provincial authority, making the legislation of that province applicable to a pension plan, and limiting the application of the PBSA. A proposed multilateral agreement is being developed through the Canadian Association of Pension Supervisory Authorities (CAPSA).
7 (1)(c)	This clarifies the definition of "administrator" and allows the employer to act as administrator for single-employer plans established by collective agreement.
7 (2)	This addition to the PBSA provides for "simplified pension plans", which, as will be prescribed by Regulation, must be administered by a financial institution. The purpose is to reduce costs and simplify administration for businesses that would not otherwise adopt a pension plan.

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Amended Sections of the PBSA	Item
10.2	This amendment requires the consent of the Superintendent before a plan's assets are transferred to another plan. This happens where plans are merged or split as a result of a sale or other business decision of an employer. Previously, the Superintendent had little control over assets being transferred. Under Section 26 of the PBSA, plan sponsors will continue to transfer the pension benefit credits of individual terminated members of a going-concern plan without the consent of the Superintendent.
18 (2)(c)	This provision provides that a pension benefit credit before retirement may be unlocked if it is less than 4 per cent of the Years Maximum Pensionable Earnings (YMPE), or such other amount as may be prescribed by the Superintendent, for the calendar year in which a member ceases to be a member of the plan or dies. The old maximum was 2 per cent of the YMPE.
23 (5)	This new subsection allows, after the death of a member or former member before retirement, the surrender of the pre-retirement benefit by the spouse in favour of a designated beneficiary as defined in the *Income Tax Act Regulations.* This addition to the PBSA reflects other legislation and was requested by both spouses and surviving spouses.
38 (1.1)	Fines and penalties have been increased to $100,000 and 12 months imprisonment for individuals and $500,000 for corporations guilty of an offence under subsection 38(1). Since the standards for registration have been eliminated, a plan need not be deregistered prior to an administrator being prosecuted. In addition, where an employer is found guilty of not remitting contributions, the court can now order the employer to remit the contributions, with interest.
7.2	This section provides for a pension council, which was previously defined as a pension committee in section 7(3) of the PBSA. A pension council may now be differentiated from a pension committee as defined in subsection 7.1(b) of the PBSA. The membership and functions of a pension council are defined in the amendment.

3. Future Amendments to the PBSA

While OSFI is not contemplating any immediate changes to the PBSA regarding same-sex benefits, an explanation on this issue is in order. Several plan sponsors have requested information following the Rosenberg decision by the Supreme Court of Ontario which found that Revenue Canada had violated the Charter of Rights by requiring beneficiaries be of the opposite sex. The government is currently reviewing all of the legislation that may be affected by the decision. In the meantime, OSFI's position on same-sex benefits remains consistent with the definition of "spouse" as currently defined in subsection 2(1) of the PBSA. Provided the PBSA definition of spouse takes priority, a plan may offer benefits to same-sex partners.

4. Amendments to the Regulations

Surplus

Many of the conditions for surplus distribution are not expected to change. For example, where an employer shows clear entitlement to surplus on plan termination, provision must be made for accrued or payable benefits before an application for surplus distribution is approved. The employer must also give notice in writing of the intention to withdraw all or part of the surplus. All plan members, former members and others entitled to a benefit must be notified and they may comment in writing to the Superintendent concerning the surplus withdrawal.

Where an employer shows clear entitlement to the surplus of a going-concern plan, the maximum surplus withdrawal is equal to the amount by which the surplus exceeds the greater of (a) two times the contribution of the employer to the normal cost of the plan, and (b) 25 per cent of the liabilities of the plan, determined in accordance with the definition of "solvency deficiency".

Where a plan does not unequivocally establish the ownership of the surplus, the amendments to the PBSA and the Regulations, are intended to facilitate agreements between plan sponsors and beneficiaries on the distribution of the surplus. First, it must be established that a surplus exists, on either a going-concern or a termination basis. For a going concern plan, the employer may then enter into an agreement with various parties with respect to surplus distribution. An agreement is recognized under the PBSA if more than two-thirds of members, former members, and other persons within a prescribed class consent. If more than one half but less than two thirds of those persons in each category consent, the employer may, for a going-concern plan, submit the proposal to arbitration. for a terminated plan, this step is obligatory.

The Regulations will describe the process for a refund of surplus application, listing those who must receive notice and the prescribed time periods for notification. The amendments will also define the arbitration process, including parties to be involved, information that must be given to interested parties and time limits. As well, the period after which the Superintendent can name an arbitrator will be set.

Disclosure

The Regulations will be amended to reflect the new PBSA requirement that additional information be disclosed to members, deferred members and retirees on an annual basis. The additional information to be disclosed includes:

- a statement setting out the right to access documents described in paragraph 28(1)(c) of the PBSA, together with a list of such documents;
- the value and description of the solvency ratio of the plan if less than one or if greater than one, may be stated as one;
- where the solvency ratio of a plan is less than one, a description of the measures the administrator has taken to bring the solvency ratio to one.

In addition to this annual information, plans sponsors must make plan texts, insurance contracts, trust agreements and financial reports filed with OSFI available to members. The amendments to the Regulations will extend the eligibility to review plan documents to former members, retirees and their spouses. The Regulations will also require that additional documents be available for review. These include:

- a written statement of investment policies and procedures in respect of the plan's portfolio of investments and loans;
- a record of all operating expenses charged to the fund for the administration of the plan, along with the purpose of each payment and the total amount paid to each payee during the year;
- a record of all direct and indirect compensation received by the administrator, any member of a board or committee acting as administrator, an actuary, an accountant, a lawyer, a notary, financial or investment adviser or other professional person for services to the plan.

Void Amendments

Regulations are being prepared to specify the conditions under which an amendment to a pension plan would be considered void. This amendment is to prevent the granting of benefits that could render a plan insolvent or jeopardize its long-term viability. In the past, a plan administrator could increase benefits regardless of the resulting deficiencies. If the plan terminated before it was solvent, benefits would be reduced in accordance with the termination priorities in the plan text. Therefore, the Regulations will specify that an amendment is void if it causes the solvency ratio of the plan to fall below a prescribed level, unless the Superintendent permits the amendment. The prescribed rate, along with alternative mechanisms to safeguard beneficiaries from undue losses, will be decided after extensive consultation has taken place over the next year.

Simplified Pension Plan

Given the low participation rate of employees of small businesses, a simplified pension plan (SPP) was proposed in the White Paper. The SPP now available under the PBSA will be similar to those in Quebec and Manitoba. The Regulations will require that SPPs be defined contribution pension plans constituted by a contract between a participating employer and a financial institution. The financial institution will be defined as the "administrator", as permitted in subsection 7(2) of the amended PBSA and must ensure that the plan complies with the legislation.

Averaging of Fees

Pension plans are required to submit a fee with Applications for Registration and Annual Information Returns. In 1991, Regulations were adopted to implement full cost recovery of OSFI's PBSA supervisory program. The legislation required that any shortfall or excess in a year be considered in setting the basic fee rate for two years out. This has resulted in substantial annual increases or decreases in fees. New Regulations will be set to average shortfalls and excesses over a period of five years which will have the effect of smoothing the changes in fees.

Supplemental Pension Plans

The amended Regulations will exempt supplemental pension plans from the application of the PBSA if under the terms of the plan to which it is supplemental, all the members of the supplemental pension plan are entitled to benefits equal to or greater than the maximum benefit or contribution limit under the *Income Tax Act*.

Since fairly extensive consultation has taken place on most of the proposed changes to the Regulations, a draft of the first round of amended Regulations will be available on the OSFI website for a limited period of time this summer. Interested parties are invited to comment. In addition, OSFI plans extensive consultation with the pension industry over the "void amendment" proposal before it becomes final. All amendments to the Regulations are expected to come into effect in 1999.

Application for Registration to Include Declaration

Applications for registration under the PBSA will be required to include a declaration that the plan complies with the PBSA and Regulations. While not part of the Regulations, OSFI has proposed a declaration to be included with both applications for registration and plan amendments. Point 3 on the form is included to ensure that any change to a plan which reduces, or has the effect of reducing, accrued benefits is approved by the Superintendent before being submitted to OSFI as an official amendment.

5. Proposed Declaration

I, ______________________________, DECLARE THAT:

1. I am a duly authorized signing officer of the Employer or a member of a board of trustees or similar body or pension committee, that is the administrator of the (name of pension plan) ____, hereinafter referred to as "the Plan";

2. The Plan, including all documents which create or support the Plan or the pension fund, complies with the *Pension Benefits Standards Act, 1985*, R.S.C. 1985, c.32 (2nd Supp.) and the regulations thereto,

   or

   The Plan as amended, including all documents which create or support the Plan or the pension fund, complies with the *Pension Benefits Standards Act, 1985*, R.S.C. 1985, c.32 (2nd Supp.) and the regulations thereto;

3. Approval by the Superintendent has been obtained for any plan amendment which has the effect of reducing pension benefits or pension benefit credits accrued before the date of the amendment; Any such amendment is null and void unless authorized by the Superintendent;

and I make this declaration conscientiously believing it to be true.

____
Date

________________________________ ____________________________________
Signature of Declarant Title or Position

6. Annual Fees for 1998-99

As explained in the section on averaging annual fees, the full cost recovery program, which was introduced in 1991, has led to dramatic fluctuations in fees. For example, the 1997/98 basic fee dropped from $10 to $8 per plan member for the first 1,000 members and from $5 to $4 per member in excess of 1,000. This was drop was the result of an excess of revenues over expenditures, payment of overdue fees and a surplus that had to be applied immediately.

Until the amendments to the PBSA become effective, the annual fees must be calculated using the old formula. For plans with a year end between October 1, 1998 and September 30, 1999, the basic fee rate, will have to increase by approximately 50 per cent over the current year, to about $12 per member for the first 1,000 members, and $6 per member for members in excess of 1,000. This will raise the minimum fee to $240 from $160 per plan and the maximum from to $80,000 from $120,000. These new rates reflect an increase in costs of delivering the program and the lack of a surplus to defray costs.

The above figures are estimates only. The actual rates will be published in the Canada Gazette before October 1, 1998.

7. List of Pension Related Items on the OSFI web site

Pension Benefits Standards Act, 1985,
Pension Benefits Standards Regulations
Directives of the Superintendent pursuant to the *Pension Benefits Standards Act, 1985*
Amendments to the *Pension Benefits Standards Act, 1985*

PBSA Annual Report, 1996
PBSA Annual Report, 1997

Annual Information Return Form
Guide to Annual Information Return
Financial Statement Form
Guide to Financial Statement Return
Current Fee Schedule

Guideline on Securities Lending - Pensions Plans, February 1992
Guideline for Converting Plans from Defined Benefit to Defined Contribution, April 1992
Memorandum to Employers Seeking Consent for a Refund Surplus, March 1993
Guideline for Plan Terminations: Defined Benefit Plans, July 1993
Guideline for Plan Terminations: Defined Contribution Plans, July 1993
Guideline for Federally Regulated Pension Plans - Derivatives Best Practices, May 1997
Supervisory Guide To Federally Regulated Pension Plans, December, 1997
Instructions for the Preparation of Actuarial Reports, October 1997
Guideline - Disclosure Best Practices, March, 1998
Guideline on Investments (Draft), April, 1998
Guideline for Governance of Federally Regulated Pension Plans, May 1998
Paper on Risk-Based Supervision of Pension Plans (Draft), May, 1998

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