Knowledge & Insights

MORNEAU SHEPELL

News & Views

Volume 13 | Issue 9
September 2016

In this issue

Ontario: Revised proposed rules on Pension Advisory Committees

On August 22, 2016, the Ontario government released revised draft regulations relating to pension advisory committees (PAC). The draft regulations clarify the previous set of draft regulations released on August 25, 2015 (see our *News & Views* of September 2015). The publication of the draft regulations seems to indicate that the government is likely to adopt new rules on PACs in the near future.

Changes in the revised regulations

The revised regulations make the following changes from the original draft:

- The period for the administrator to provide notice of a vote to establish an advisory committee after a member request has been extended from 60 to 90 days;
- The information to be distributed to members and retirees by the administrator on behalf of those requesting an advisory committee is restricted to a description of the purposes of an advisory committee, as set out in legislation. The previous requirement to transmit information was more open-ended;
- It is now specified that the member and retiree vote to establish a PAC must be secret;
- It is now specified that the member and retiree vote may be held electronically, by mail, or via an in-person ballot;
- The PAC is to meet to discuss administrative matters at least twice annually, unless it determines that an annual meeting is sufficient;
- The period during which an administrator is exempt from holding a subsequent vote if the vote to establish a PAC is unsuccessful is extended from two to three years.

Conclusion

The revisions to the draft PAC regulation will make the requirements on plan administrators somewhat less onerous, but the requirements regarding the establishment and operation of a PAC are still fairly onerous. It remains to be seen if members and retirees will take advantage of the new provisions to attempt to establish a PAC.

Public comments are requested by **September 12, 2016.**

British Columbia: Union consent for conversions to target benefit plans

In August 2016, the Financial Institutions Commission of British Columbia (FICOM) released Bulletin 16-006 titled "Clarification of Union Consent Requirement for Target Benefit Plan Conversions" (the "Bulletin"). The Bulletin is a follow-up to a previous FICOM Bulletin, "Guideline for Converting Plans from Defined Benefit to Targeted Benefit", which provided guidance to plan administrators considering a conversion from a defined benefit to a target benefit plan structure (see our *News & Views* of April 2016).

In this Bulletin, FICOM clarifies the requirement for union consent when a plan provision is converted to a target benefit provision. Pursuant to section 20(2)(d) of the *Pension Benefits Standards Act* a plan administrator may amend a negotiated cost multi-employer pension plan to convert a defined benefit provision to a target benefit provision (which may reduce accrued benefits) only if the union representing members consents.

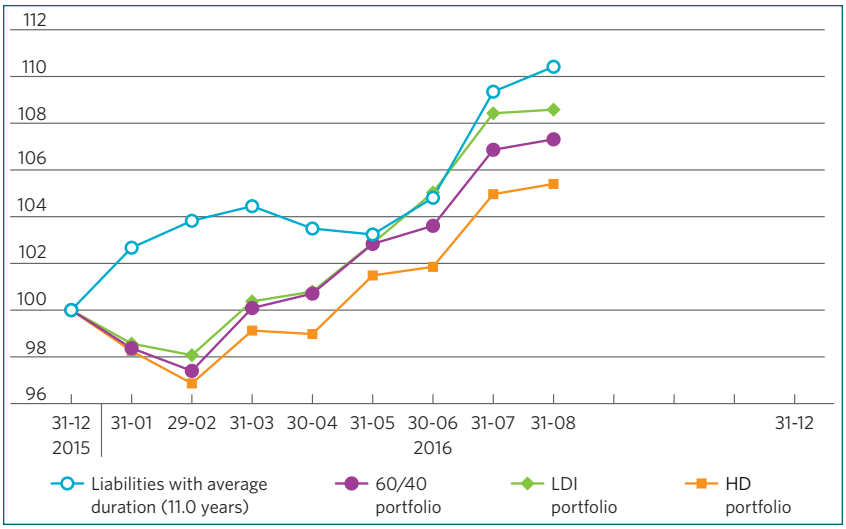
FICOM states that the requirement for union consent relates to benefits accrued prior to the effective date of the conversion. Therefore, if the plan amendment provides that benefits accrued to the date of conversion may not be reduced at any time without the consent of the Superintendent, union consent is not required. However, if all benefits are converted to a target benefit provision and may be reduced in the future without the consent of the Superintendent, union consent is required.

Upon filing an amendment for a conversion to a target benefit provision which requires union consent, the plan administrator will be required to provide confirmation that the union has consented to the conversion. FICOM has amended its plan amendment submission form to include this requirement.

Tracking the funded status of pension plans as at August 31, 2016

This graph shows the changes in the financial position of a typical defined benefit plan with an average duration since December 31, 2015. For this illustration, assets and liabilities of the plan were each arbitrarily set at $100 million as at December 31, 2015. The estimate of the solvency liabilities reflects the new CIA guidance published in August 2016 for valuations effective June 30, 2016 or later. The following graph shows the impact of three typical portfolios on plan assets and the effect of interest rate changes on solvency liabilities of medium duration.

The evolution of the financial situation of pension plans since December 31, 2015

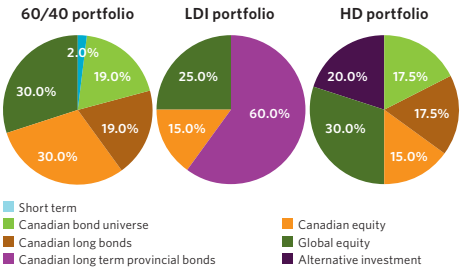


During the month of August, Canadian universe bonds, Canadian long term bonds, Canadian and global equity markets and alternative investments showed positive returns, while Canadian long-term provincial bonds showed negative returns. With a return of 0.4%, the 60/40 portfolio as well as the highly diversified portfolio (HD) outperformed the low volatility portfolio (LDI) (0.1%). The underperformance of the LDI portfolio is explained by the allocation in Canadian long-term provincial bonds and a lower weight in global equity markets. Annuity purchase rates and the rates used in the calculation of solvency liabilities slightly decreased during the month, increasing the solvency liabilities by 1.0% for a medium duration plan. For this type of plan, an investment in either of the 60/40, the LDI or the HD portfolio resulted in a slight decrease in the solvency ratio. The table below shows the impact of past returns on plan assets and the effect of interest rate changes on solvency liabilities of a medium duration plan, based on the plan's initial solvency ratio as at December 31, 2015 as well as the asset allocation of the three typical portfolios.

Initial solvency ratio as at December 31, 2015	Evolution of the solvency ratio as at August 31, 2016 for three different portfolios		
	60/40 portfolio	Low volatility portfolio (LDI)	Highly diversified portfolio
100%	97.2%	98.3%	95.5%
90%	87.5%	88.5%	85.9%
80%	77.8%	78.7%	76.4%
70%	68.0%	68.8%	66.8%
60%	58.3%	59.0%	57.3%

Comments

1. No consideration has been made for contributions paid to the plan or for benefits paid out of the plan.
2. Solvency liabilities are projected using the rates prescribed by the Canadian Institute of Actuaries (CIA) for the purpose of determining pension commuted values.
3. The underlying typical defined benefit plan is a final average plan with no pension indexing, including active and inactive participants representing 60% and 40% of liabilities, respectively.
4. Assets are shown at full market value. Returns on assets are based on three typical benchmark portfolios.



Since the beginning of the year, driven by strong returns within the Canadian equity and the Canadian fixed income markets, the 60/40 portfolio, the LDI portfolio and the HD portfolio returned 7.3%, 8.6% and 5.4% respectively. The solvency liabilities increased over that same period between 9.5% and 10.9% depending on the duration of the group of retirees. The variation in the plan's solvency ratio as at August 31, 2016 stands between -4.5% and -1.7%.

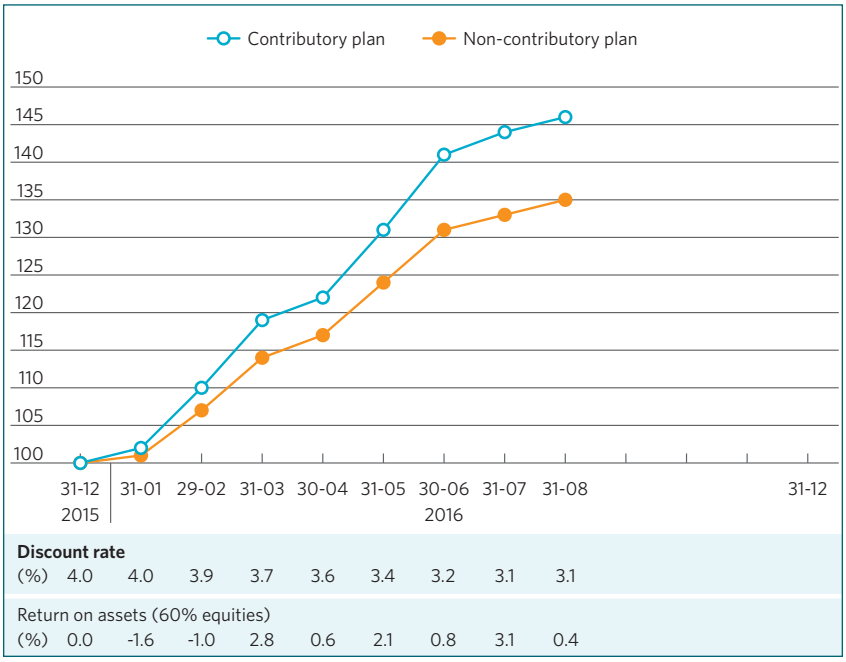
Please contact your Morneau Shepell consultant for a customized analysis of your pension plan.

Impact on pension expense under international accounting as at August 31, 2016

Every year, companies must establish an expense for their defined benefit pension plans.

The graph shows the expense impact for a typical pension plan that starts the year at an arbitrary value of 100 (expense index). The expense is influenced by changes in the discount rate based on high quality corporate and provincial (adjusted) bonds and the median return of pension fund assets.

Expense Index from December 31, 2015



The table below shows the discount rates for varying durations and the change since the beginning of the year. A plan's duration generally varies between 10 (mature plan) and 20 (young plan).

Discount rate

Duration	December 2015	August 2016	Change in 2016
11	3.71%	2.93%	-78 bps
14	3.91%	3.05%	-86 bps
17	4.04%	3.11%	-93 bps
20	4.12%	3.15%	-97 bps

Since the beginning of the year, the pension expense has increased by 46% (for a contributory plan) due to the decrease in the discount rate.

Comments

1. The expense is established as at December 31, 2015, based on the average financial position of the pension plans used in our *2015 Survey of Economic Assumptions in Accounting for Pensions and Other Post-Retirement Benefits* report (i.e. a ratio of assets to obligation value of 91% as at December 31, 2014).
2. The return on assets corresponds to the return on the Morneau Shepell benchmark portfolio (60% equities and 40% fixed income).
3. The actuarial obligation is that of a final average earnings plan, without indexing (two scenarios: with and without employee contributions).

Please contact your Morneau Shepell consultant for a customized analysis of your pension plan.

MORNEAU SHEPELL

Contributing editors

Glorie Alfred, J.D., LL.M.
Pension Legislation

Andrew Zur, LL.B.
Pension Legislation

Morneau Shepell is the only human resources consulting and technology company that takes an integrative approach to employee assistance, health, benefits and retirement needs. The Company is the leading provider of employee and family assistance programs, as well as the largest administrator of retirement and benefits plans and the largest provider of integrated absence management solutions in Canada. Through health and productivity, administrative, and retirement solutions, Morneau Shepell helps clients reduce costs, increase employee productivity and improve their competitive position. Established in 1966, Morneau Shepell serves approximately 20,000 clients, ranging from small businesses to some of the largest corporations and associations in North America. With almost 4,000 employees in offices across North America, Morneau Shepell provides services to organizations across Canada, in the United States, and around the globe. Morneau Shepell is a publicly-traded company on the Toronto Stock Exchange (TSX: MSI)

morneaushepell.com

@Morneau_Shepell

Morneau Shepell

MENTAL HEALTH PARTNER