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Medical marijuana: A smoking hot topic for health and benefit plans

Bill C-45 (*Cannabis Act*) created quite a stir in April 2017 when it was introduced to the House of Commons. The bill's intention is to create a framework to control the production, distribution, sale and possession of cannabis in Canada. It should be noted that the *Cannabis Act* focuses on recreational marijuana and is not expected to change the way individuals access cannabis for medical purposes. Even though Bill C-45 is still under review, it could become effective by July 1, 2018 should it be approved.

Canadian legislation surrounding medical marijuana has changed dramatically over the years. Access to cannabis for medical purposes was first permitted in Canada in 1999 under Section 56 of the *Controlled Drugs and Substances Act*. The Minister of Health had the authority to grant special exemptions to individuals who were suffering and dying from debilitating illnesses. However, it was still generally considered a crime to possess cannabis in Canada at this time.

Since then, several important court cases—along with changes in societal opinion—have contributed to changes in Canadian legislation. Today, medical marijuana can be obtained through a health practitioner's prescription and bought from a licensed producer. However, this begs the question: can employees claim medical cannabis under their group health and benefit plan?

Medical marijuana and benefit plans

In most cases, for a drug to be reimbursed as an eligible expense under a group benefit plan in Canada, a Drug Identification Number (DIN) is required. In order for a drug to be sold and receive a DIN, Health Canada must review and approve its safety, efficacy and quality against the standards of the *Food and Drug Act* and its regulations. To date, cannabis is not an approved therapeutic drug in Canada and does not have a DIN. While carriers may reject claims under this basis for fully insured plans, some self-funded administrative services only (ASO) plans may have more flexibility in choosing what is to be covered under their plans. Since the employer is the one paying the claims and the carrier is only administering the plan, ASO plans may have more flexibility to tailor their decisions.

While medical marijuana is generally not eligible under a group extended healthcare benefit, it can be acceptable as a healthcare spending account (HSA) expense. Since the regulations for HSA expenses rely on the guidelines of the Canada Revenue Agency—and specifically expenses that are eligible under the Medical Expense Tax Credit—medical marijuana is generally an eligible expense through a HSA.

Special cases in Canada

Recently, there have been some plans that have covered medical marijuana for a variety of reasons. Notable employer decisions and exceptions include the following:

- A student at the University of Waterloo was successful in having the health insurance provider cover his medical marijuana in 2014. This was approved based on the student's medical evidence, the financial impact on the plan and how the coverage affects the student's personal and academic well-being.
- In 2017, the Nova Scotia Human Rights Commission determined that prescribed medical marijuana for a Nova Scotia man must be covered by the Canadian Elevator Industry Welfare Trust Plan (a multi-employer plan).
- Loblaws and Shoppers Drug Mart recently announced the addition of medical marijuana to their benefit plan with a $1,500 annual maximum. Claims will only be considered for prescriptions to treat symptoms of multiple sclerosis and side effects of chemotherapy.
- Ontario Public Service Employees Union (OPSEU) announced the addition of medical marijuana to their benefits plan on June 15, 2017, with a $3,000 annual maximum. There are no medical condition limitations.
- In an effort to reduce opioid use and addiction, an Ontario construction union, LiUNA! Local 625, extended coverage for medical cannabis to its retired, disabled workers and dependents.

Conclusion

With the likely legalization of recreational marijuana looming, an increasing number of individuals view medical cannabis as an acceptable form of treatment, which can drive a benefit plan's usage up. Undoubtedly, the pressure is likely to increase on plan sponsors to provide coverage and the potential cost impact for marijuana could be significant. Insurance companies are still hesitant to provide specifics on the projected cost impact, citing a lack of credible data. Nonetheless, the estimated cost of a regular marijuana user is projected to be around $10,000 per year. Beyond group benefits, medical marijuana in the workplace raises a number of concerns for employers and relevant policies should be proactively reviewed or created.

British Columbia: Reduction in provincial medical premiums

In the 2017 budget update tabled on September 11, 2017, the British Columbia government announced that Medical Services Plan (MSP) premiums will be reduced by 50% for all residents effective January 1, 2018. This change could result in savings of $450 per year for individuals and $900 per year for families currently paying full premiums. MSP premiums are based on annual net household income and the net income threshold at which individuals are fully exempt from paying MSP premiums will increase from $24,000 to $26,000, while couples with two children and family net income below $35,000 will also be exempt.

BC is unique in collecting monthly premiums from individuals to fund health care as other provinces do so through income or employer payroll taxes; however, in many cases, employers pay at least a portion of those premiums for their employees. MSP premiums had been increasing by 4% annually for the last number of years, up to January 1, 2017, when the premium structure was revised to no longer consider the number of children and the 4% increase was cancelled (see our *News & Views* of March 2017).

The government has also announced that it will establish a task force to recommend the best way to eliminate MSP premiums and replace lost revenue. The task force will report back to government in the Spring of 2018, with the target date for elimination of the premiums in four years. This is a more specific timeframe for the elimination of MSP premiums than was announced earlier in the year as the previous government had stated that the timing would be "influenced by the Province's fiscal capacity".

Unlike the previous government's announcement earlier in 2017, the MSP reduction is not contingent on household income or any other criteria. No application will be required to obtain the 50% reduction in MSP premiums and the adjustment will apply to all BC residents. In cases where BC employers pay at least a portion of MSP premiums on behalf of their employees, the reduction and future elimination of MSP premiums is favourable for employers, but it remains to be seen what measures will be enacted to replace this revenue source for government. Those employees will receive a lower taxable benefit while employers stand to gain from the premium savings. Employers should review employment contracts and collective agreements to determine the specific impact of this change. Employers may also proactively consider the planned elimination of MSP premiums within four years in their total compensation strategy.

Nova Scotia announces consultation on DB pension plan funding

On September 6, 2017, Nova Scotia announced a consultation on defined benefit (DB) pension plan funding and other regulatory matters. Broadly speaking, the three options under consideration are:

1. maintain full solvency funding with measures to help reduce funding volatility;

2. eliminate solvency funding and enhance going concern funding; and

3. require only partial funding of solvency liabilities.

Background

In August 2017, Nova Scotia announced two forms of temporary solvency funding relief (see our *News & Views* of September 2017). This follows previous rounds of temporary funding relief in 2009 and 2013. Furthermore, the new *Pension Benefits Act* adopted on June 1, 2015, permitted some permanent measures to relieve funding requirements, such as allowing the deferral of new special payments until 12 months after a valuation date, permitting smoothing of solvency interest rates, and permitting letters of credit (LOCs) of up to 15% of solvency liabilities.

Options under consideration

Three options are considered in the consultation paper:

1. Maintain full solvency funding

Solvency liabilities would still have to be 100% funded, but some or all of the following relief measures would be introduced to help reduce the volatility and variability of funding payments:

Longer funding period: The maximum funding period could be increased from five years to a longer period, such as seven or ten years.

Consolidate solvency deficiencies: Instead of requiring different schedules for each solvency deficiency established in a valuation report, deficiencies could be consolidated and a single 5-year schedule produced at each valuation date.

Solvency reserve accounts: A separate account within a pension plan fund could be established to hold payments made in respect of a solvency deficiency. Employer withdrawals from a solvency reserve account could be made, up to a certain maximum, if the solvency ratio was greater than 100%.

Letters of credit: LOCs obtained from a financial institution can currently be used to cover solvency special payments for up to 15% of solvency liabilities. The 15% cap on LOCs could be raised.

2. Eliminate solvency funding and enhance going concern funding

Under these proposals, solvency funding would be eliminated, but enhanced going concern funding requirements would be adopted. These enhanced going concern funding requirements could include some or all of the following features:

Require a funding reserve or Provision for Adverse Deviation (PfAD): Requiring an amount in excess of a plan's liabilities to be funded before the plan may take an action that could weaken the plan's funded position.

Shortened funding period: Provide for a shorter maximum funding period than the current 15-year period.

Return on investment assumptions: The maximum allowed interest rate for use in going concern valuations could be required to be based on high-quality long term corporate bonds.

Solvency "trigger" for enhanced funding: A plan's solvency position would be used to determine whether additional funding is needed or if the plan would be allowed to take an action that would weaken its funded position. For example, if a plan fell below a certain solvency funding threshold, then a requirement to pay an additional lump sum could be triggered.

3. Reduced solvency funding requirements

The solvency funding requirement would be reduced to a lower level, such as 85% of solvency liabilities. This reduced solvency funding approach could be combined with elements of the other two options described above.

Other regulatory issues

The consultation paper also requests feedback on several other potential regulatory reforms affecting Nova Scotia DB pension plans.

Target benefit plans

Nova Scotia's pension legislation contains provisions that have not been proclaimed into force that would permit target benefit plans to be

established in unionized settings. This is similar to Ontario's legislation, which is also unproclaimed. The paper asks whether Nova Scotia should develop a target benefit pension plan framework, whether it should be restricted to unionized environments, and whether past benefits should be convertible to target benefits.

Annuity discharge

Under this proposal, a statutory discharge would be provided to DB plan sponsors who purchase annuities from life insurance companies to meet their pension obligations. Certain conditions would have to be met to qualify for the discharge.

Permitted investment rules

In 2015, the federal government amended its investment regulations. In particular, they were amended so that the 10% limit on investing pension plan assets in a single entity be based on the "market value" of a pension plan's assets rather than the "book value." Nova Scotia is asking whether it should adopt the 2015 federal amendments, and if its pension regulations should be amended to incorporate the federal investment regulations by reference.

Conclusion

The Nova Scotia consultation will be of interest to employers who sponsor Nova Scotia-registered DB pension plans. The consultation follows the introduction of target benefit plans in New Brunswick, Quebec funding reforms, and the newly announced funding framework in Ontario.

Public comments are requested by **November 10, 2017**.

Update: New Brunswick adopts funding relief regulation

On September 29, 2017, the New Brunswick government adopted a funding relief regulation for multi-jurisdictional pension plans. The relief regulation provides a 10-year extension to solvency funding requirements, as well as a consolidation of past deficiencies. A multi-jurisdictional pension plan is defined as a pension plan registered in New Brunswick with members subject to the jurisdiction of other provinces.

The final version of the regulation is identical to the draft regulation (see our *News & Views* of September 2017), with one significant exception. The draft regulation required a single notice to be sent to plan members when solvency relief was elected, while the final version removes that requirement.

However, the new regulation includes a new requirement that notice be included in each annual statement to members until the expiry of the 10-year period. The notice must show why the administrator elected funding relief and provide a 10-year comparison of required contributions both before and after funding relief measures. The notice must also be provided to former members and others with an entitlement in the plan, despite the fact that New Brunswick does not require annual statements to be sent to former and retired members.

The administrator is required to provide the Superintendent with a copy of the notice provided on an annual basis until the end of the 10-year period.

Saskatchewan: New funding rules for pension plans with fixed contributions

Effective August 25, 2017, the *Saskatchewan Pension Benefits Regulations* were amended to establish a new funding and regulatory regime for limited liability plans (LLPs). An LLP is a private sector pension plan to which contributions are limited by collective agreement or plan documents. The

regulations follow a consultation on negotiated cost pension plans that was held in 2016 (see the July 2016 edition of *News and Views*).

In general, the new funding and regulatory regime for LLPs is as follows:

- A permanent exemption from funding solvency deficiencies, although solvency deficiencies still have to be calculated;
- Going concern deficiencies to be funded over 15 years;
- A provision for adverse deviations (PfAD) to be calculated on the basis of the equity allocation of the LLP, with the PfAD to be funded for current service costs starting with the second actuarial valuation report;
- Restrictions on benefit improvements;
- Possibility of calculating commuted values based on the plan's going concern assumptions and decreasing the commuted value to the funded position of the plan, when the commuted value is transferred from the plan; and
- Enhanced member communications.

The Saskatchewan Financial and Consumer Affairs Authority has issued a detailed guide to LLPs.

Commentary

The Saskatchewan announcement on LLPs will directly affect a small number of Saskatchewan-registered pension plans. However, it is of interest to see Canadian jurisdictions continue to develop new plan models. The LLP could be considered something of a cross between a standard multi-employer pension plan and a target benefit plan (TBP). It borrows several significant ideas from recent reforms in Canada, particularly the TBP framework in Alberta and British Columbia, namely the switch to "going-concern plus" funding approach and the option for plans to switch to a new commuted value calculation framework.

Ontario: Regulation on administrative penalties

On September 15, 2017, Ontario filed a regulation setting the amounts for administrative penalties levied under the *Pension Benefits Act* (the "Act"). Administrative penalties will come into force on January 1, 2018.

This follows the release of a draft regulation in May 2017 (see the June 2017 edition of *News and Views*).

The Act was amended in November 2016 to permit the Superintendent of Financial Services (the "Superintendent") to impose administrative penalties on plan administrators and other persons without requiring a prosecution and conviction for a provincial offence.

There will be two types of penalties, each subject to different types of fines. A "general administrative penalty" would be imposed for non-compliance with a substantive requirement of the PBA, while a "summary administrative penalty" would be imposed for failing to make required regulatory filings in accordance with regulatory deadlines. A summary administrative penalty would be subject to daily penalties of $100 or $200, subject to a $10,000 maximum for individuals and a $25,000 maximum for corporations. A general administrative penalty would have no daily penalty and the same $10,000 maximum for individuals and a $25,000 maximum for corporations would apply.

Comparison with the draft regulations

The basic approach set out in the draft regulations has stayed the same. The final version of the regulation makes a few changes to the draft regulation, namely:

- Breaches of the general standard of care applicable to pension plan administrators are no longer subject to administrative penalties;
- Breaches of rules respecting letters of credit are no longer subject to administrative penalties;

- Certain actions, such as late filings of pension plan amendments and late issuance of marriage breakdown notices, are no longer subject to summary administrative penalties and daily accrual, although they are still subject to general administrative penalties.

Impact of administrative penalties

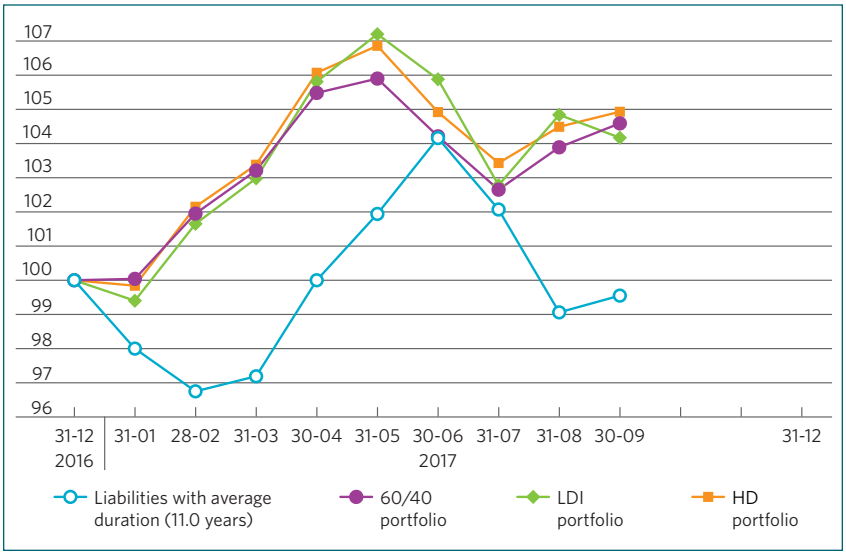
When the new rules come into force, administrative penalties will be of significant concern to plan administrators and service providers. The potential amount of administrative penalties can be significant, especially for late filings subject to daily accrual under summary administrative penalties.

Furthermore, until now the potential for a prosecution for violations of the Act has been somewhat remote and reserved for the most serious cases. Administrative penalties can be imposed much more easily on plan administrators, and the onus will be on the recipient to file an appeal with the Financial Services Tribunal of Ontario within 15 days of receipt of the penalty notice. If no appeal is filed, payment is required within 30 days of receipt of the penalty notice. It should be noted that administrators will not be permitted to pay administrative penalties from the pension fund.

Tracking the funded status of pension plans as at September 30, 2017

This graph shows the changes in the financial position of a typical defined benefit plan with an average duration since December 31, 2016. For this illustration, assets and liabilities of the plan were each arbitrarily set at $100 million as at December 31, 2016. The estimate of the solvency liabilities reflects the new CIA guidance for valuations effective June 30, 2017 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, 2016



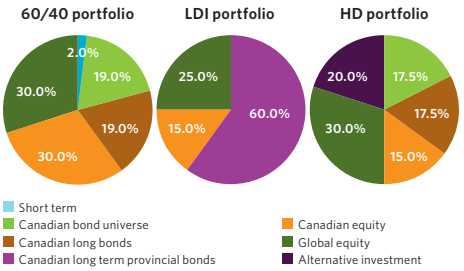
During the month of September, Canadian universe bonds, Canadian long term bonds and Canadian long-term provincial bonds showed negative returns while Canadian and global equity markets (CAD), as well as alternative investments, showed positive returns. With a return of 0.7%, the 60/40 portfolio outperformed the highly diversified portfolio (HD) (0.4%) and the low volatility portfolio (LDI[1]) (-0.6%). The relative outperformance of the 60/40 portfolio is mainly due to its bigger allocation to Canadian and global equity markets. The prescribed CIA Annuity purchase rates increased during the month; however, the commuted value rates used in the calculation of solvency liabilities decreased. As a result, the solvency liabilities increased by 0.5% for a medium duration plan. For this type of plan, an investment in the 60/40 portfolio resulted in a solvency ratio increase while an investment in the LDI or the HD portfolio resulted in a solvency ratio decrease.

Initial solvency ratio as at December 31, 2016	Evolution of the solvency ratio as at September 30, 2017 for three different portfolios		
	60/40 portfolio	Low volatility portfolio (LDI)	Highly diversified portfolio
100%	105.1%	104.6%	105.4%
90%	94.6%	94.2%	94.9%
80%	84.0%	83.7%	84.3%
70%	73.5%	73.3%	73.8%
60%	63.0%	62.8%	63.2%

[1] Liability driven investment

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.



The table 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, 2016 as well as the asset allocation of the three typical portfolios. Since the beginning of the year, driven by strong returns in global equity markets as well as the alternative investments, the 60/40 portfolio, the LDI portfolio and the HD portfolio returned 4.6%, 4.2% and 4.9% respectively. The solvency liabilities decreased over that same period from 0.4% to 0.6% depending on the duration of the group of retirees. The variation in the plan's solvency ratio as at September 30, 2017 stands between 2.8% and 5.4%.

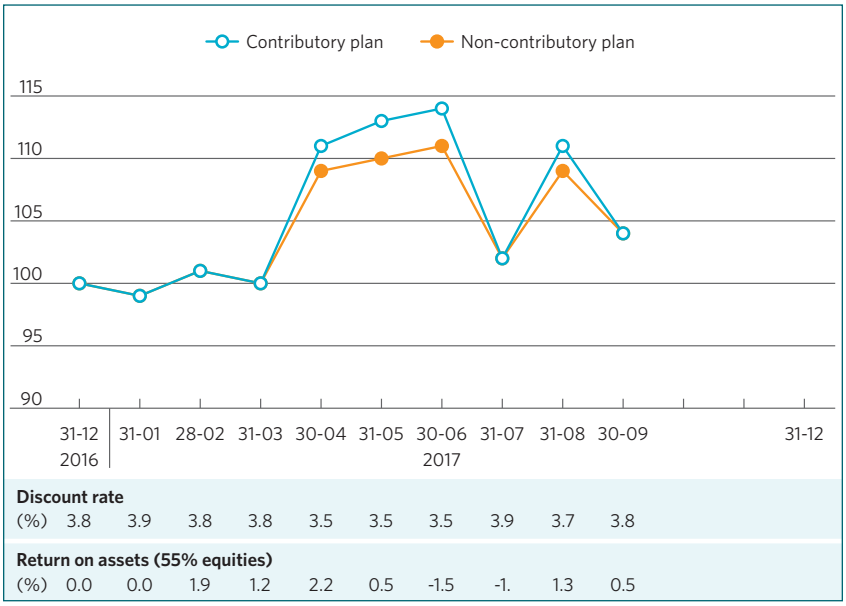
Please contact your Morneau Shepell consultant for a customized analysis of your pension plan.

Impact on pension expense under international accounting as at September 30, 2017

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, 2016



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 2016	September 2017	Change in 2017
11	3.66%	3.67%	+1 pdb
14	3.81%	3.80%	-1 pdb
17	3.90%	3.88%	-2 pdb
20	3.96%	3.93%	-3 pdb

The discount rate has increased in the last month, resulting in a reduced expense, bringing it almost to its level at the beginning of the year.

Comments

1. The expense is established as at December 31, 2016, based on the average financial position of the pension plans used in our *2016 Survey of Economic Assumptions in Accounting for Pensions and Other Post-Retirement Benefits report* (i.e. a ratio of assets to obligation value of 94% as at December 31, 2015).
2. The return on assets corresponds to the return on the Morneau Shepell benchmark portfolio (55% equities and 45% fixed income), which reflects the average asset mix in our 2016 Survey.
3. The actuarial obligation is that of a final average earnings plan, without indexing (two scenarios: with and without employee contributions).

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