



2011 TRENDS

Blakes
CANADIAN LAWYERS

PENSION & EMPLOYEE BENEFITS

ACTION ON REFORM

Ontario: In 2010, the Ontario legislature passed Bill 236 and Bill 120 which brought much needed reform to the Ontario *Pension Benefits Act* (PBA). Some of the changes to the PBA were effective immediately, such as clarifying the surplus entitlement provisions. Other changes, such as eliminating partial wind-ups, implementing immediate vesting, addressing the transfer of surplus in corporate transactions and the introduction of phased retirement, will take effect on a future (to be determined) date. We expect that many of these provisions will come into effect in 2011 along with the corresponding regulations. As the old adage goes, "the devil is in the details," and we expect such details to be released in 2011.

Federal: Similarly, the federal government amended the *Pension Benefits Standards Act, 1985* (PBSA) in 2010, and we anticipate further changes in the form of new regulations in 2011. Significantly, the federal government eliminated the quantitative limits in respect of real property and Canadian resource property investments by pension funds. Ontario has indicated that it intends to amend the PBA regulations to mirror the changes to the federal investment rules, whereas certain other provinces (i.e., Alberta, British Columbia, Saskatchewan and Manitoba) adopted these revised rules automatically.

The federal government has indicated its intention to further amend the investment rules by modifying the 10 per cent single-issuer investment limit and prohibiting investment in securities of the sponsoring employer. In addition, there has been significant lobbying by the pension industry for the removal of other quantitative investment restrictions that, if adopted, would make investments in venture capital, private equity and infrastructure by pension plans much more straightforward.

MORE REFORM

Pooled Registered Pension Plans (PRPPs): In December 2010, the federal Minister of Finance proposed the creation of a new type of private pension plan, the PRPP. PRPPs involve the pooling of pensions provided by multiple employers and the self-employed, with plan investment and administration handled by a third-party administrator. The federal government has expressed a desire to adopt the legislative changes necessary to establish PRPPs, in 2011. Many provinces appear to support the concept of PRPPs, and it will be interesting to see more details regarding how these plans will work.

Canada Pension Plan (CPP): Meetings between federal and provincial finance ministers to discuss pension issues are expected to continue in 2011 and changes to the CPP will undoubtedly be a topic of discussion. With the proposal to establish PRPPs (discussed above) now on the table, it is unclear whether the political will to amend the CPP to increase contribution rates and benefits exists. While some provinces continue to support CPP reform, either in conjunction with the creation of PRPPs or on its own, there is some concern the time is not right to increase CPP contributions.

Prince Edward Island: Pension legislation has been released for comment, and we expect that 2011 will bring PEI its first pension benefits statute.

New Brunswick: Following in the footsteps of other provinces, the Government of New Brunswick has appointed an expert panel to study pensions. The panel will examine how to ensure private pensions are protected and sustainable in the long term.

STOCK OPTIONS

Tax changes have been implemented that eliminate the stock option benefit deferral election and tighten the withholding rules relating to the exercise of stock options and other types of equity compensation awards. The new legislation also eliminates the 50 per cent employee stock option deduction (available with respect to many employee stock options and designed to give capital gains-like tax treatment on the option benefit) in respect of stock option cash-outs unless the employer elects to forego its deduction in respect of the cash-out payment. Now, either the employee can claim the 50 per cent deduction or the employer can claim a deduction of the cash-out payment, but not both.

With respect to the deferral election that permitted an employee to defer inclusion in employment income of stock option benefits relating to publicly traded shares until the year in which the employee sold the underlying shares, such election is no longer available for any stock option exercised after March 4, 2010.

Effective for stock options exercised after 2010, an employer will be required to make withholdings from an employee's remuneration determined on the hypothetical basis that the deemed employment benefit arising from the exercise of the options is paid to the employee as a cash bonus. The legislation does not address what would happen if the amount of the employee's cash remuneration is not sufficient to fund the

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withholding obligation, although employees holding options on publicly traded shares may be able to sell their shares immediately upon exercise to fund the tax withholding. These changes may create a greater incentive on the part of many employees to dispose of shares acquired through an exercise of options in order to pay the corresponding tax liability. We expect that 2011 will bring about changes to the design and administration of many companies' equity incentive plans in light of the new tax rules.

NON-RESIDENT TRUST RULES

In August 2010, the Department of Finance released revised draft legislation that reflects the changes to the non-resident trust (NRT) proposals announced in the March 2010 federal budget. The changes are good news for sponsors and administrators of deferred-income plans and other tax-exempt entities. In particular, the draft legislation contains an exemption from the NRT rules for all persons exempt from tax under section 149(1) of the *Income Tax Act* (Canada), including registered pension plans, elected master trusts and various tax-exempt corporations.

TREATMENT OF SURPLUS IN CORPORATE TRANSACTIONS

The unanimous Supreme Court of Canada (SCC) decision in *Burke v. Hudson's Bay Co.* determined that, based on the specific plan documentation at issue, there was no obligation on the vendor to transfer any portion of surplus pension plan assets on the sale of the business. However, the SCC stated that the "resolution of the issue of surplus transfer when the pension plan documents indicate that employees are entitled to surplus on plan termination is best left to another case where that issue arises." The effect of the *Burke* decision in Ontario will only be temporary since recent amendments to the PBA will require a pro-rata share of surplus to be transferred in the context of a sale of a business, although the regulations setting out the applicable conditions have not yet been released. In other provinces that do not expressly require surplus to be transferred on the sale of a business, the *Burke* decision results in legal uncertainty as to whether surplus needs to be transferred if the employees have legal entitlement to the surplus.

RE: INDALEX

The *Re: Indalex* case was heard by the Ontario Court of Appeal in November 2010 and a decision is expected in 2011. This case deals with the issue of whether pension plan funding deficits are subject to a deemed trust under the PBA and, therefore, may have priority over other creditors of the plan sponsor. This is a very important case to watch as it could significantly affect the ability of defined benefit plan sponsors to obtain financing if the Court of Appeal overturns the lower court's decision and finds that pension plan deficits are subject to a deemed trust.

GLOBAL COMPENSATION PRACTICES

In response to the global financial crisis, the leaders of the G20 established the Financial Stability Board to develop and implement strong regulatory, supervisory and other policies in the interest of global financial stability. The federal Minister of Finance requested that members of the Canadian Bankers Association comply with the Financial Stability Board's Principles of Sound Compensation Practices and it will be interesting to see whether the *Income Tax Act* (Canada) will be amended to permit such compliance or whether the Canada Revenue Agency will develop policies surrounding the implementation of such principles.