

If My Company Sponsors A DC Pension Plan, Will We Need To Participate In The ORPP?



We assumed the answer was no. Now it's not so clear.

What is the ORPP?

The Ontario Retirement Pension Plan (ORPP) is an unprecedented, Ontario-only, mandatory provincial pension plan intended to provide pension coverage to working Ontarians without workplace pension plans. Starting in 2017, affected employees and employers in Ontario will be required to contribute an equal amount to the ORPP, capped at 1.9 percent each (3.8 percent combined), on an employee's annual earnings up to \$90,000.

The Ontario Budget and the ORPP

The 2014 Ontario Budget¹ stated that:

Since the ORPP is intended to assist individuals most at risk of undersaving, particularly middle-income earners without workplace pensions, those already participating in a comparable workplace pension plan would not be required to enrol in the ORPP.

Since defined benefit (DB) pension plans, defined contribution (DC) pension plans, and multi-employer pension plans (MEPPs)², as defined under the Ontario *Pension Benefits Act* (PBA), are all employee pension plans registered under the PBA, the assumption made by many in the pension industry was that the Ontario Budget's reference to comparable workplace pension plans would include DB plans, DC plans and MEPPs.

Ontario's ORPP Legislation and Consultation Paper

On December 8, 2014, the Ontario government introduced its proposed ORPP legislation, and on December 17, 2014, released a Consultation Paper inviting feedback on the ORPP's key design details. Public input on the Consultation Paper was required to be provided by February 13, 2015.

A key issue of the ORPP's design details being considered as part of the Consultation Paper is the plan types that will fall within the definition of comparable workplace pension plans. Employers with a comparable workplace pension plan will be exempt from participating in the ORPP. In the Consultation Paper, the Ontario government has indicated a preference for the view that DB plans and MEPPs constitute comparable workplace pension plans, but that DC plans will not constitute comparable workplace pension plans. Does this mean that employers currently offering DC pension plans must also participate in the ORPP? The question is a significant one since DC pension plans are increasingly the norm in Ontario, including among employers who previously provided a DB plan for their employees and have either closed or terminated their DB plan (or the DB component of their plan).

What is the Best Definition of a Comparable Workplace Pension Plan?

Ontario's Consultation Paper sets out the following features as the ORPP key features:

1. mandatory employer contributions;
2. locked-in funds;
3. benefit provided for life;
4. indexation to inflation; and
5. pooled investment risk.

Notwithstanding the fact that the proposed ORPP includes all five features listed above, in our view, if a plan meets the criteria under both (1) and (2) above, namely, if the plan has mandatory employer contributions and the benefits are locked-in (locked-in means that plan members cannot withdraw their retirement funds but they must be used to provide a retirement income), then the plan should constitute a comparable workplace pension plan.

DB plans, DC plans and MEPPS all satisfy the conditions under (1) and (2). Group registered retirement savings plans, deferred profit sharing plans and pooled registered pension plans do **not** meet the conditions under (1) and (2) and should not therefore, in our view, constitute comparable workplace pension plans. The remaining features in (3) to (5) above (and in particular, (4) and (5)), while perhaps desirable from a policy perspective, do not constitute the standard framework necessary for a workplace pension plan and therefore should not be required features of a comparable workplace pension plan.

Similarly, under the PBA, a plan must satisfy the features in (1) and (2) above in order to qualify for registration as an employee pension plan. This means that DB plans, DC plans and MEPPs all constitute pension plans under the PBA. The PBA imposes minimum standards on these plans, thereby affording members considerable protection with respect to their benefits. Further, based on the terms of the PBA, whether or not a plan satisfies the criteria under (3) to (5) has no impact on its qualification as a registered pension plan. Although the

primary objective of all pension plans is to provide periodic payments for the lifetime of the plan member, the PBA permits transfers to other vehicles that may or may not provide a benefit for life. The ability to mitigate longevity risk is, however, available to members through the purchase of annuities from an insurance company.

While the Consultation Paper indicates a preferred approach that all DB plans and MEPPs meet the definition of a comparable workplace pension plan, we note that many single-employer DB plans and MEPPs themselves do not meet all criteria under (1) to (5) above. Most private sector DB plans and MEPPs do not, in fact, index benefits to inflation, so most of these plans would not satisfy the criteria under (4) above.

Furthermore, members of a DB plan or a MEPP who have terminated employment or plan membership may elect to, and often choose to, transfer the commuted value of their pensions to a prescribed retirement savings arrangement, which, like a DC pension plan, does not meet the conditions under (3) to (5) above.

DC Plans

While the Consultation Paper's preferred approach is to exclude DC plans from the definition of a comparable workplace pension plan, a question asked in the Consultation Paper is whether there are circumstances under which DC plans should be considered comparable workplace pension plans. Would establishing a minimum employee/employer contribution rate for DC plans make DC plans comparable?

In our view, a DC plan with a minimum employee/employer contribution rate of 1.9 percent for employees and 1.9 percent for employers (for a 3.8 percent total contribution rate), thereby mirroring the proposed ORPP contribution rates, should be considered a comparable workplace pension plan. For DC plans where either no employee contributions are required or the minimum employee contribution rate is less than 1.9 percent, then the total employer contribution rate, or the total employee/employer contribution rate, as applicable, should be, at a minimum, 3.8 percent.

We note that DC plans must provide for a minimum employer contribution of one percent of members' earnings in order to be eligible for registration as a pension plan under the *Income Tax Act* (Canada). For most DC plans, however, both employee and employer contributions are required, and it is our experience that the majority of employer-sponsored DC plans have a total contribution rate that is at least four percent, with the employer-required contributions usually as high as, or higher than, the employee required contributions.

If Ontario were to take the position that:

1. DC plans do not constitute a comparable workplace pension plan and thereby require DC plan sponsors to also participate in the ORPP; or that
2. only a DC plan with a total required contribution of 10 percent, for example, constitutes a comparable workplace pension plan,

then some DC plan sponsors in Ontario could choose to amend their DC plan to offset their employer contributions in future by their required ORPP contributions, or more likely, could choose to abandon their employer-sponsored DC pension plans altogether.

A further question posed in the Consultation Paper is whether requiring members to convert a portion of their savings in a DC plan to an annuity upon retirement would make a DC plan a comparable workplace pension plan. We do not think it would be desirable for a member's DC plan savings to have to be converted into an annuity in order for a DC plan to be considered a comparable workplace pension plan. Since the price of annuities fluctuates greatly with interest rates, imposing such a requirement could subject DC plan members to an unreasonable level of risk related to the level of interest rates at the time of their retirement.

Summary

As suggested above, a significant number of private sector employers in Ontario with registered pension plans have either closed or frozen their DB plans and now offer only DC plans for their new hires. The Ontario government's Consultation Paper informs us that the government would prefer not to consider these DC plans, regardless of the level of contributions, to be comparable workplace pension plans. For the reasons discussed above, we disagree with this approach. In our view, DB pension plans, DC pension plans (at least those having a minimum combined employee and employer contribution level equivalent to that of the ORPP) and MEPPs should all meet the definition of comparable workplace pension plans for purposes of being exempt from participating in the ORPP. If Ontario excludes DC plans from comparable workplace pension plans, then this may have unintended negative consequences for the members of those plans, since many employers may simply terminate their DC plans rather than incur the additional financial cost of ORPP mandatory participation in addition to the costs of their employer-sponsored pension plans. Simply put, we hope to see DC pension plans included in the definition of comparable workplace pension plans.