Special Notice

January 27, 2020

Another step to improving Ontarians' financial security in retirement

In releasing multiple regulations detailing rules regarding variable benefit accounts for pension plans, Ontario finally joins the majority of provinces allowing members to decumulate directly from their defined contribution (DC) pension plan. This welcomed change will allow DC plan members to benefit from plan sponsor oversight and low fees during their spend-down years, which will increase the amount of retirement income they are able to generate. Variable payments directly from the plan also help to simplify the transition from accumulation to decumulation. These regulations already exist federally as well as in all other provinces except for Newfoundland and Labrador, New Brunswick and PEI.

Amendments to the Regulations provide guidance on requirements and restrictions with respect to the payment of variable pension benefits pursuant to the *Pension Benefits Act* (PBA) and *Regulation 909 (General) of the Revised Regulations of Ontario* (Reg. 909), changes to insurance contracts with deferred or life annuities, and treatment of variable annuities in family law matters. Highlights of the regulations and their impact are discussed below.

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Regulation 368/19: Variable benefit payments from a pension plan

Regulation 368/19 was published on November 23, 2019, and reviews the prescribed requirements and restrictions governing the payment of variable pension benefits.

Basic rules regarding variable benefit accounts

Pension plan members may elect to receive variable benefits from their pension plan by delivering a directive to the plan administrator to establish a variable benefit account for the member pursuant to Reg. 909. The regulations provide for a member to move all of their DC savings to a variable account. If a plan sponsor has allowed more flexibility in their plan document, a plan member may elect to allocate some of the DC savings to variable benefit while allocating the remainder to an annuity or other option.

Payments from a variable benefit account can only be made once in a calendar year unless the pension plan permits payments on a more frequent basis. Variable payments will mirror the life income fund (LIF) withdrawal rules and will allow for up to 50% unlocking of pension benefits upon a transfer to an RRSP or a cash withdrawal within 60 days of opening a variable benefit account. Retired members would be required to apply to the plan administrator for the 50% unlocking of funds.

Once a retired member receives an initial statement regarding their variable benefit account, they must notify the administrator in writing to:

- Unlock funds (up to the 50% maximum allowed);
- Confirm the amount of income to be paid out of the variable benefit account in respect of the calendar year, subject to minimum and maximum limits under the *Income Tax Act of Canada (ITA)* as if the variable benefit were a LIF;
- Stipulate the frequency of the payments to be made, if the pension plan permits more than one payment per calendar year; and
- Confirm the method of payment.

If the retired member does not notify the administrator in writing within 120 days of receiving their initial statement, the administrator shall pay to the retired member an amount equal to the minimum amount required under the ITA and continue to pay the minimum amount until receiving written direction from the retired member.

Members are entitled to notify the administrator in writing of any change in the amount to be paid, frequency of payment (if permitted by the pension plan), and method of payment at least once in a calendar year.

Transfers in and out of variable benefit accounts

The following retirement savings arrangements can be used to transfer funds to a variable benefit account:

- Life income funds;
- Locked-in retirement accounts; and
- Locked-in retirement income funds.

Transfers out of a variable benefit account can be made to life income funds and locked-in retirement accounts. An insurance contract for the purchase of a life annuity may be used if it meets the requirements for insurance contracts under section 22 of Reg. 909.

Initial and annual statements

The *Regulation* sets out the requirements for initial and annual statements for variable benefit accounts for retired members and specified beneficiaries.

All statements must include the name of the pension plan and its provincial registration number; the amount and nature of the fees and expenses, if any, charged to the variable benefit account during the calendar year; and the retired member's or specified beneficiary's name and date of birth. Additional information that may be prescribed, depending on whether the statement is the initial or annual statement for the retired member or specified beneficiary, includes:

- A description of the benefits to be provided on the death of a retired member or specified beneficiary;
- Statements regarding the designation of beneficiaries;
- An explanation of the prescribed notice requirements;
- The balance of the variable benefit account at the beginning and end of the calendar year for annual statements to retired members; and
- The balance of the variable benefit account on the retired member's date of death and the balance of the account on the date of the initial statement for specified beneficiaries.

Regulation 369/19: Changes to transfer rules related to insurance

Regulation 369/19 amends the *PBA and Regulation 909*, revising the transfer rules related to insurance contracts providing deferred or immediate life annuities to include transfers from a retired member's variable benefit account. It also provides details on the required information a plan administrator must provide to members regarding their variable benefits, including:

- Statements on transfers of pension funds to a variable benefit account;
- Minimum and maximum limits on the amount of income that may be paid out of a variable benefit account in a calendar year;
- Estimates of the amount in a member's defined contribution account at their retirement date; and
- A statement informing the member of their rights to notify the plan administrator of changes to the frequency of payments out of a variable benefit account or the amount of income to be paid.

Regulation 370/19: Variable benefits and family law valuations

Regulation 370/19 amending *Ontario Regulation 287/11* adds rules regarding the application of the *Family Law Rules* to variable benefits for family law valuation purposes. The new rules include details with respect to:

- Preliminary valuations;
- Shortened life expectancy;
- Imputed values for family law purposes; and
- Transfers of lump sums for family law purposes.

Regulation 370/19 states that if, as of the family law valuation date, a retired member is receiving payment of variable benefits and pension benefits under a defined benefit or defined contribution pension plan, the preliminary and imputed values of the member's pension benefits are determined separately for the variable benefits and the defined benefit or defined contribution benefits. The preliminary value of the funds in a retired member's variable benefit account is the balance in the retired member's variable benefit account as of the family law valuation date.

Coming into force

The new regulations came into force on January 1, 2020 upon proclamation of section 2 of Schedule 34 to the *Building Ontario Up Act (Budget Measures), 2015*.

Impact:

The changes will allow DC pension plan members in Canada's largest province to continue to benefit from a group-buying arrangement through their spend-down years. The magnitude of the benefit from the reduced fees plan members pay in a group arrangement compared to individual accounts must not be underestimated. In many cases, reduced fees can result in six to seven additional years of retirement income, or an increase in retirement income of between 25% and 30%. Moreover, the benefit of plan sponsor oversight with respect to plan investments provides a significant level of comfort for plan members. Additionally, given that retirees typically have larger account balances, plan sponsors that allow retired members to remain in their plans help ensure that all of their members (active and inactive) can benefit from economies of scale that often result in reduced fees and other favourable price reductions. It's a win for members both while accumulating and decumulating.

With Ontario joining the other provinces that currently allow for variable payments, we may see a considerable number of pension plans with members across Canada implement variable payments. Plan sponsors with national membership were hesitant to implement a decumulation strategy that only applied to some of their members. The change may now act as a catalyst for the remaining provinces to introduce the required legislation and regulation as well.

Many plan sponsors who have begun their discussion and review of decumulation options for their members worry about the lengthening of their fiduciary responsibility for a plan member's lifetime. However, given that most provinces now allow for variable payments, governmental encouragement–and the mechanisms to allow plan sponsors to support their members through retirement–has increased substantially. Plan sponsors who choose not to provide this support to plan members may find that the pendulum has swung the other way, and not using their buying power may open them up to new scrutiny and liability.

For plan sponsors who decide to move forward, key pieces of the regulations determine some of the administrative components of variable benefits such as: how frequently members can receive income during a calendar year and whether to allow retirees to divide their DC balances between variable payments and other vehicles such as annuities.

More than four years following the announcement about variable payments in the 2015 budget, we are pleased that the regulations have been implemented and the provincial government has taken a significant step towards improving Ontarians' financial security.

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