Today's Objectives

- To discuss terms and conditions of pension plans

Recall that:

Terms and Conditions of Pension Plans

- A pension plan is a legal promise and principal provisions relate to:
  1. Eligibility
  2. Pension formula
  3. Credited or pensionable service
  4. Employee contributions
  5. Retirement Age
  6. "Normal" and Optional Pension Forms
  7. Pre-retirement Death Benefits
  8. Termination Benefits
  9. Disability Benefits
  10. Inflation Protection

Example – Pension Formula – Integration with CPP

- An employee has pensionable earnings of $75,000 and is entitled to the maximum CPP retirement pension payable in 2020, which is $14,110. She has worked 35 years for her employer and retires at age 65.
- Her employer's pension plan goal is for employees to receive up to 70% of pre-retirement income through integration with the CPP. The pension formula is 1.3% of earnings up to the YMPE and 2% of earnings in excess of the YMPE. The YMPE in 2020 is $58,700.

a) What amount of income will the employee receive from her employer's pension and the CPP?

b) Suppose instead that the employee is 61 years of age with 35 years of service and she is able to retire with an unreduced pension. What bridge benefit will her pension provide to age 65?

1. Registered Pension Plans (RPPs)

Terms and Conditions of Pension Plans

8. Termination Benefits
   - The benefits and rights of the e'ee upon termination of employment other than by death or retirement must be clearly defined in the plan document
   - E'ee always gets back his/her own contributions with interest
   - If e'ee is fully vested he/she can receive either
     - A deferred annuity
     - The commuted value of the deferred annuity, which then must transferred to a locked-in vehicle
   - More on this later

1. Registered Pension Plans (RPPs)

Terms and Conditions of Pension Plans

9. Disability Benefits
   - A clear definition of disability for purposes of the plan is required
   - Most plans have some form of short-term and/or long-term disability coverage (definitions very detailed)
   - If the employer has a benefit plan that provides short or long-term benefits, the pension plan does not need to pay benefits but the employee may continue to accrue service in the plan
   - If the employer does not have a benefit plan that provides short or long-term disability benefits, the pension plan may provide an immediate unreduced pension

1. Registered Pension Plans (RPPs)

Terms and Conditions of Pension Plans

10. Inflation Protection
    - There is no absolute requirement for inflation protection
    - Some plans have implicit protection pre-retirement – e.g. Final average earnings DB
    - With DC plans, as long as returns rise with or exceed inflation the e'ee is protected
    - For other plan types (DB - career average plan, flat benefit plan) only 'protection' is benefit enhancements/updates
    - Many plans have/do make ad hoc adjustments post-retirement
    - Public sector plans often provide some form of post-retirement inflation protection (e.g. indexed payments), details of which would be in their plan document

1. Registered Pension Plans (RPPs)

Terminology and Comments on Pension Plans

- Provincial legislation varies by province, many are comparable to Ontario though
- **Legislation is set to protect plan members interests**

- Vesting
  - If a plan member is **vested**, this **means that they are entitled to the portion of the pension benefit provided by e'er contributions**
  - E'ee contributions always refundable, credited with interest
  - The maximum time to be fully vested is 24 months, most plans require less time than that and/or immediate vesting
  - In Quebec, since 2001 all RPPs must have full vesting as soon as e'ee joins the plan andOntario also now requires full vesting as soon as e'ee joins plan (since 2012)

1. Registered Pension Plans (RPPs)

Terminology and Comments on Pension Plans

- Locked In
  - **"Locked in" means that the vested entitlement must provide retirement income****, i.e., the e'ee can't withdraw any contributions or portion of the pension benefit in cash prior to retirement
    - The benefit at termination can only be received in the form of retirement income (from the pension or other locked in account)
    - In Ontario the locking-in rules tend to be the same as vesting rules
  - This means if you terminate after being fully vested (and locked in), **you cannot access your RPP money until you retire and have reached NRA, i.e., the money is 'locked in'**
    - Two benefits for $$ being locked in:
      - provides for income at retirement
      - plus creditors cannot seize locked in money

** some exceptions may be made for financial hardship

1. Registered Pension Plans (RPPs)

Terminology and Comments on Pension Plans

- Locked In
  - **Portability means that the commuted value of a terminating employee's pension may be transferred, on a locked in basis, to another RPP or some other locked in Retirement savings arrangement** (and there are no tax consequences)
  - In Ontario the commuted value can be transferred to
    - Another RPP (if the other plan allows)
    - 'Locked in' RRSP
    - Locked in Retirement Account (LIRA)
    - LIF - Life Income Fund (age 55 or higher)
    - Deferred Life Annuity (payments starting at NRA or within 10 years of NRA)

Module 2 – Old Age
→ Group or Employer Plans (Ch 1, 3, 9 and 14 of *Morneau Shepell Handbook*)

1. Registered Pension Plans (RPPs)

Terminology and Comments on Pension Plans

- What Happens when plan member retires?
  - All pensions are payable for the life of the plan member (e'ee)
  - What is paid **depends on the "normal" pension form (or optional form if elected)**
  - If the e'ee has a spouse then
    - The pension must be a joint and survivor (J&S) annuity
    - These annuities are such that payment drops to usually 60% of the initial amount if the plan member dies first
    - E'ee can opt out of J&S annuity only if spouse signs a waiver
  - If the e'ee does not have a spouse then
    - The pension (life annuity) has no guarantee period OR
    - A guarantee period of no more than 15 years

1. Registered Pension Plans (RPPs)

Terminology and Comments on Pension Plans

- What Happens if plan member dies before retirement?
  - This **depends on whether the plan member was vested**
  - If he/she dies before being vested
    - only e'ee contributions are refunded with interest to the beneficiary
  - If he/she dies after being vested
    - Most provinces require 100% of commuted pension value to be paid to the spouse or beneficiary (or estate) if no spouse
    - Spouse has the option to take the commuted value as:
      i. a lump sum (locked in)
      ii. deferred pension
      iii. immediate pension

1. Registered Pension Plans (RPPs)

Terminology and Comments on Pension Plans

- What Happens if plan member dies after retirement?
  - This **depends on what pension form was elected**
  - If joint and survivor annuity was the pension form:
    - payments will drop from 100% to (usually) 60% and spouse will receive these payments for as long as they live
  - If a guaranteed life annuity was the pension form
    - if death occurs after guarantee period, nothing is paid
    - if death occurs during the guarantee period, remaining guaranteed payments paid to the beneficiary
  - If a life annuity with no guarantee was the pension form
    - nothing is paid

1. Registered Pension Plans (RPPs)

RPP Examples - Website links

1. OMERS - Defined Benefit Plan

   https://www.omers.com/Members/myOMERS

   – Provides 2% of ‘best 5 years salary’ × YOS, indexed benefits

2. Western - Defined Contribution Plans

   https://www.uwo.ca/hr/form_doc/pension/doc/plan_info/plan_summary.pdf

   – Faculty or academic plan: e’er contributes 8.5% of salary, e’ee can choose 1.5 of 5.5% of salary plus make voluntary contributions (up to overall combined maximum of 18% salary)

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1. Registered Pension Plans (RPPs)

RPP Examples - Website links

1. OMERS - Defined Benefit Plan
   https://www.omers.com/Members/myOMERS
   - **A great example of a large public Defined Benefit Plan**
   - **Reviewing plan also helps pull together RPP lecture topics**
   - **Points of interest on the OMERS webpage**
     - Members handbook (28 page pdf file), plan overview section
     - Actual contribution rates not in handbook (but see website link)
   - You should have an understanding of;
     - Who is covered under the plan
     - Benefit formula, Indexing
     - Contributions (is a contributory plan)-required and voluntary
     - CPP integration
     - NRA, ERA - Reduced & Unreduced Early Retirement benefits
     - Vesting, Locked In, Termination, Portability
     - Disability and Death Benefits

1. Registered Pension Plans (RPPs)

RPP Examples - Website links

2. Western - Defined Contribution Plans
   https://www.uwo.ca/hr/form_doc/pension/doc/plan_info/plan_summary.pdf
   - **A great example of a large Defined Contribution plan**
   - **Reviewing plan also helps pull together RPP lecture topics**
   - You should have an understanding of;
     - The fact that there are different plans for different employee groups-academic and admin plans
     - Contribution rates vary by plan and there is some consideration of YOS in factors
     - Required e'ee contributions (some choice in faculty plan)
     - Voluntary contributions
     - NRA, ERA
     - Vesting, Locked In, Termination, Portability
     - Disability and Death Benefits

2. Group RRSPs

- This is another type of Employer Plan
- Group RRSPs have gained in popularity over the years as an alternative to RPPs
  - key reason for this is that they are not subject to pension standards legislation

- Advantages of Group RRSPs (to whom in each case?)
  - No plan text to be registered with authorities
  - No locking-in of contributions
  - More flexibility to vary contributions among plan members
  - No restriction on who can be the beneficiary
  - No mandatory joint-and-survivor pension on retirement
  - Do not have to buy a life annuity on retirement

2. Group RRSPs

- Disadvantages of Group RRSPs
  - Employer contributions are considered salary to the e'ee and this can increase employer's payroll costs (CPP, employment insurance, etc.)
  - Employer cannot be certain that the accumulated funds in a group RRSP will be used by the e'ee to provide a retirement income
  - Employer contributions are immediately vested

- For an employee, Group RRSPs have advantages over Individual RRSPs including the fact that
  - Group RRSP contributions are done by payroll deduction (convenience)
  - E'ee can benefit from the greater purchasing power and investment opportunity of a larger group(e.g. lower investment management fees than on individual RRSPs)

2. <u>Group RRSPs</u>

- Group RRSP's often used on a stand-alone basis (no RPP offered by an e'er), but are also used by some employers as a supplement to a non-contributory defined benefit RPP

- Many group RRSP's have very low or no e'er contributions because:
  - E'er contributions are immediately vested
  - E'er contributions are considered salary to the e'ee

- Contributions to a group RRSP are tax deductible (for e'ee) but will reduce maximum contribution room for the employee's individual RRSP