Pension Protection Act:

Considerations and Implications

What does the new Pension Protection Act mean for you?

Experts discuss the impact and opportunities after the government announced new rules for defined benefit pensions.

The introduction of the Pension Protection Act (PPA) this year has prompted pension plan sponsors to reassess their risk appetite, investment, and funding strategies.

The PPA prioritizes unfunded defined benefit pension liabilities over most other creditors, including those who are secured, should an employer become insolvent or go bankrupt.

While helping to protect retiree pension benefits, concerns have been raised about its potential to adversely influence the borrowing costs and habits of employers with defined benefit schemes.

To discuss these issues and more, several experienced professionals participated in a recent webinar that focused on the consequences and possibilities for plan sponsors.

Hosted by **Kristyn Dougall** of **Benefits and Pensions Monitor**, the webinar was titled **Pension Protection Act: Considerations and Implications**, sponsored by **CAAT Pension Plan**.

Dougall was joined by moderator **Alistair Almeida**, Segment Lead, Asset Owners at **CIBC Mellon; Kelly Bourassa,** Partner and Calgary Leader, Restructuring & Insolvency Group at **Blake, Cassels & Graydon LLP;** and **Andrew Whale,** Vice President, Strategic Risk Management at **CAAT Pension Plan**.

Almeida kicked off the discussion by noting that while Canada's pension plans have a global reputation for strong management and resilience, they are facing many of the same pressures that other plans are seeing around the world.

"Regulatory change is a constant theme in our industry," Almeida says. "But I think we can see that these changes are accelerating in impact and scope."

Bourassa agrees, noting that the new Act is just the latest development in a series of new protections for pensioners in insolvency proceedings. In 2008 amendments enhanced protections for the amounts to be paid by the employer under a Defined Contribution Plan.

Then in 2012, amendments included amounts to be paid by employers to the administrator of a pooled registered pension plan.

"Now we come to the Pension Protection Act," Bourassa says. "And the PPA has an immediate impact on any new prescribed pension plans."

Turning to Whale, VP at CAAT Pension Plan, moderator Almeida asked how this impact would unfold for different stakeholders.

The Act applies to any registered pension plan that's regulated by the federal and provincial governments, Whale says. That includes the sponsors of single employer pension plans.

"However," Whale adds, "there is a well-argued viewpoint that confidently demonstrates why the Act wouldn't apply to jointly sponsored pension plans such as the CAAT pension plan."

Before expanding on this point, Whale says it's useful to consider the context of the Act and why the government felt it needed to make changes. Whale asked Bourassa to speak to the history of insolvencies in Canada.

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"There are approximately 9,000 defined benefit plans in Canada, and those plans have approximately 4.5 million members," Bourassa explained. "In the past 14 years, there have been only 10 insolvency cases where pensions were reduced due to an employer's insolvency."

Those reductions affected about 50,000 individuals across the country, Bourassa says. That equates to approximately 0.1% of Canadians. So, while these cases affected a very small share of pension holders, the PPA is expected to have broad implications for many, Bourassa adds.

"The concern from my perspective and others," Bourassa says, "is that the legislation may in fact have a negative effect overall on employees – and potentially make defined benefit plans less available than they are now."

Asked to detail some of the implications of the Act, Bourassa added that employers will need to prepare themselves. The legislation, she says, forces companies who participate in prescribed plans very likely to increase their reporting to lenders and investors.

"The problem from a lender's perspective, which impacts the plan sponsors, is that the funded status is constantly changing, and constant change creates uncertainty. Lenders do not like uncertainty.

"There could be a restricted access to capital or an increased cost of capital for pension sponsors. Lenders may require they obtain some kind of insurance or create a trust to ensure any deficiency which is likely to cut into cash flow and other short-term cash needs."

Whale shares these concerns, noting that there are a host of solutions available for employers who are looking to de-risk and avoid implications of the Act, such as merging a defined benefit pension plan with a jointly sponsored pension plan.

"In many ways this is really the same discussion plan sponsors have been having - around general de-risking of their balance sheets and simplifying internal operations - for years," he says. "And this really just adds another catalyst to those conversations." One unfortunate result could be many plans moving away from defined benefit pensions towards capital accumulation plans, which they may otherwise have not wanted to, he adds.

"The reality of a bill intended to protect pensions is that it could ultimately result in fewer Canadians participating in defined benefit plans. It really comes down to what problem employers are trying to solve, and what kind of retirement benefits they want to offer going forward."

The option of merging with a jointly sponsored plan would allow employers to continue maintaining a DB plan as a part of their total rewards offering, while reducing their risk and eliminating the alternative of purchasing expensive annuities.

Bourassa notes that a number of concerns were raised about the Act but fell on deaf ears, which now means that they're going to have to be interpreted by the courts.

"The Act doesn't specify what type of plan," she says. "How does it apply to a multi-employer Pension Plan? How do you quantify the deficiency of things like this? These are all going to be left for courts to decide in real, live cases with real live people – which is not the way that you really want to leave these things." **BPM**

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