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# The employee benefits landscape in Canada

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Canadians are living longer and facing increased responsibility to save for their retirement. Because life expectancies are on the rise, retirement savings will have to last longer. This, and other economic factors, are placing pressures on the Canadian retirement income system and its traditional defined benefit (DB) and defined contribution (DC) plan designs. Employers doing business in Canada need to be aware of the evolving legal environment in relation to employee benefits in Canada, and pension plans in particular, as more and more employees will be looking to their employers for retirement solutions. In this chapter we consider two of the three pillars supporting retirement income in Canada – government sponsored retirement benefit plans and employer sponsored retirement plans.

## Government social security benefit plans

Government sponsored retirement benefit plans are considered as one of the three pillars supporting retirement income in Canada – the other two being employer sponsored retirement plans (discussed below) and the individual's own retirement savings. Employer sponsored retirement plans are often presented to employees in this context. The Government sponsored retirement benefit plans consist of the Canada Pension Plan (or, if the employee resides in Québec, the almost identical Québec Pension Plan) (CPP/QPP), Old Age Security (OAS) and the Guaranteed Income Supplement (GIS).

### (i) OAS and GIS

No employee or employer contributions are required for either of OAS or GIS. Entitlement to the GIS benefit is means-tested. Entitlement to the OAS benefit is not means-tested up-front, but it is subject to a "clawback" based on an income threshold. For the period between July 2017 to June 2018, OAS pension is reduced if the annual net income of a person is more than $74,788 and it is entirely clawed back once a person has an annual net income of $121,314.

### (ii) CPP/QPP

Both employees and employers are required to contribute to either the CPP or QPP (as applicable) based on the "year's maximum pensionable earnings" (YMPE) up to certain maximums. In 2018, for example, the YMPE is $55,900. For CPP, the employer and employee each contribute 4.95% of earnings per year, for a total of $2,593.80 per year for each of them. Under the QPP, the employer and employee each contribute 5.4% of earnings, for a total of $2,829.60 per year for each of them. Upon retirement, CPP/QPP provides benefits that are intended to replace 25% of the employee's average earnings up to the YMPE. The exact amount of pension will depend on an employee's average earnings, the years of participation and the retirement age. In 2018, the maximum benefit under the CPP and QPP is $1,134.17 for an employee who retires at age 65.

Many employers design their retirement plan so as to integrate the benefits that employees will receive under the CPP/QPP and the benefits payable under the employer's retirement plan (*i.e.* the contributions required and the benefits payable under the employer plan will take into account CPP/QPP contributions and benefits).

The legislation governing the CPP was amended in 2016 to implement the first major reform since its implementation in 1966. Commencing in 2019, the benefit levels under the CPP will increase gradually. The income replacement ratio will increase from 25% to 33.33% of pensionable earnings, from the first dollar earned up to an increased YMPE (projected to be equal to roughly $82,700 in 2025). The exact increase will depend on how much and for how long an employee has contributed to the enhanced CPP. A worker will get the full increase after contributing to the enhanced CPP for 40 years. Both employer and employee contributors will, however, also increase to fund this enhancement. These increased contributions will be phased in over a 7 years period, commencing in 2019. The QPP will be enhanced in the same way as the CPP.

Employer and employee contributions will increase in order to fund the enhancements. Increased contributions will be phased in over a seven-year period commencing in 2019.

### (iii) EI

In Canada there is also an Employment Insurance (EI) program that provides unemployment benefits for qualifying individuals. Employers and employees are required to contribute towards EI based on the amount of "insurable earnings" ($51,700 in 2018) up to certain maximums.

## Employer sponsored retirement plans

Benefit plans provided by employers for their Canadian employees are typically divided into two broad categories: (i) group benefit (welfare) plans, and (ii) pension and retirement savings arrangements. The second category can be further divided between the following sub-categories: (a) registered pension plans, (b) other registered retirement arrangements and (c) unregistered retirement plans (typically supplemental plans). The legal framework that overlays these employee benefit plans depends on the type of employee benefit plan, whether federal or provincial governments have jurisdiction over the employment relationship and the province in which the individual is employed.

Subject to one small exception in Québec (see below), there is currently no legislative requirement for employers to establish or participate in any type of retirement plan for the benefit of their employees (i.e., it is a voluntary system). However, where employers establish retirement plans for their employees, the employer must comply with the governing legislative requirements.

For employers with Québec employees, the *Voluntary Retirement Savings Plan Act* requires an employer to provide a Voluntary Retirement Savings Plan (VRSP) to employees if the employer does not provide to its employees, a registered pension plan or a registered retirement savings plan or a Tax Free Savings Account Plan. Employers are not, however, required to contribute to a VRSP.

### Registered pension plans

Pension plans that qualify as "registered pension plans" are subject to minimum standards legislation and income tax legislation. In Canada, there is no single piece of legislation which

sets pension standards rules for all registered pension plans (e.g., like ERISA in the U.S.). Instead, the federal government and nine of the 10 provinces have their own minimum pension standards legislation (note that Prince Edward Island does not yet have minimum standards pension legislation). The pension plan must comply with the legislated minimum standards of the applicable jurisdiction(s) with respect to covered employees and with the requirements under the *Income Tax Act* (ITA).

As is the case in relation to labour and employment law, the level of government that has jurisdiction regarding minimum standards pension legislation is determined by the industry in which an employer operates and is the same jurisdiction that applies for the purposes of labour and employment law. The majority of employers in Canada fall under provincial jurisdiction. In these cases, the applicable provincial jurisdiction that governs pension plan minimum standards is usually the jurisdiction where the employee works.

Where the employer has employees in more than one Canadian jurisdiction, the laws of multiple jurisdictions may apply with respect to a single registered pension plan. There is a lack of uniformity in the minimum standards legislation across the country and this has a significant impact on how pensions are managed in Canada. Nevertheless, while such minimum standards legislation is not identical and important differences do exist, the minimum standards legislation generally imposes similar requirements in respect of such things as eligibility for membership; locking in; the need for regulator consent for pension plan asset transfers; duties of plan sponsors and administrators; and pension plan investments. It is noteworthy that recent changes have resulted in important differences in the funding requirement across the various jurisdictions.

In addition, the interpretation of registered pension plan documents and legislation is governed by the common law (except in the province of Québec as detailed below). As a result, the roles, obligations, liabilities and entitlements of plan sponsors, plan administrators, plan members and trustees of pension funds are shaped and affected by the applicable legislation, the plan documents and the common law.

## Common law

The administration of a pension plan and underlying documents that create a pension plan (i.e., the pension plan rules and trust agreements) are also subject to the common law (other than in Quebec). Accordingly, the terms of the plan documents, as interpreted through the common law, may prevail to provide greater rights to members than those provided for under pension legislation or otherwise govern the employer's rights or responsibilities with respect to the plan. For example, common law imposes fiduciary duties on plan administrators. These duties require an administrator to act in the best interests of the plan members and avoid conflicts of interest among other things. The duty also comprises the duty to act with an even hand, the duty of loyalty, and the duty to exercise the appropriate knowledge and skill in its role as administrator.

## Québec

In Québec, the *Civil Code of Québec* (CCQ) sets out the substantive law applicable in the province, subject to specific statute law. Accordingly, where Québec is the applicable jurisdiction, the administration of employer-sponsored registered pension plans will generally be governed by the minimum standards legislation applicable in that province. However, specific issues, such as fiduciary obligations, will also require the application of the CCQ.

## Income Tax Act

In addition to complying with applicable minimum standards pension legislation, a pension plan must be registered under the federal ITA in order to qualify for preferential tax treatment. Essentially, the ITA limits the amount that may be contributed to a registered pension plan on a tax-sheltered basis and limits the benefits that may be paid from a registered pension plan.

## Retirement savings arrangements

In addition to, or as an alternative to, a registered pension plan, an employer may sponsor other types of retirement savings arrangements, such as group registered retirement savings plans (Group RRSPs), deferred profit sharing plans (DPSPs) and group tax-free savings accounts (TFSAs). These plans are defined contribution in nature, and contributions are typically invested at the direction of the employees and the benefits payable are typically equal to the balance of the member's account.

While Group RRSPs, DPSPs and TFSAs are not subject to minimum standards regulation, they are regulated by the ITA. Among other things, the ITA prescribes the maximum contribution limits applicable to such plans.

While no minimum standards legislation applies to Group RRSP, DPSPs and TFSAs, there are guidelines published by regulators overseeing the financial services sectors, which may apply and set the standard to which such plans should be administered.

Another type of retirement savings arrangement is the pooled registered pension plan (PRPP) (known as voluntary retirement savings plans in Quebec). These plans are also defined contribution arrangements, but individuals' assets are pooled, so a PRPP should be able to offer investment and savings opportunities at lower administration costs. Unlike Group RRSP, DPSPs and TFSAs, PRPPs are subject to minimum standards legislation.

# Unregistered retirement plans

## Supplemental plans

An employer may establish a supplemental plan for certain employees to "top-up" their pension plan benefits. Such plans typically provide benefits above the ITA limits applicable to registered pension plans and they are not subject to minimum standards legislation. For example, the maximum benefit accrual rate is capped at 2% and the maximum annual DB limit in 2018 is $2,944.44 per year of service. If a person is accruing defined benefits under a registered plan with a 2% accrual rate, he or she will maximize accruals under the plan for 2018 once he or she has earned pensionable earnings of $147,222 (since 2% of $147,222 equals $2,944.44). The pension of an employee with 30 years of service would be capped at $88,333 per year under the registered plan ($2,944.44 x 30 years of service).

A higher pension is possible if the employer has set up a supplemental plan. Where such a plan is funded or secured in some fashion, it may be subject to classification under the ITA as a "retirement compensation arrangement" and will be subject to particular tax requirements.

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### Non-registered DC plans

Employers may also provide a non-registered plan to receive defined contribution amounts in excess of amounts permitted under the ITA limits in respect of registered plans. These types of non-registered plans are typically provided in conjunction with Group RRSPs and/or DPSPs. Contributions to these plans are not tax deductible to the employee and income earned in these plans is not tax exempt.

## Other employee benefit plans

### Health and welfare benefits

In addition to sponsoring pension and retirement savings arrangements, employers may offer health and welfare benefit plans to their employees, on an insured, self-insured or partially insured basis. These benefits vary widely among employers and in general, there is no legislation which regulates the provision of benefits under these plans. Thus, these employer plans generally are not (as such) subject to minimum standards legislation. It is important to note, however, that both employment standards legislation (which requires the continuation of benefits during applicable statutory leaves) and human rights legislation (which forbids discrimination based on prohibited grounds) do apply.

Typical health and welfare benefits include life insurance, accidental death and dismemberment insurance, long-term disability, short-term disability, health care and dental care. Because Canada currently has a system of universal health care, private health care benefits offered by employers are typically top-up benefits covering such expenses as semi-private or private hospital care, drugs and vision care.

## Collective bargaining regime

In a unionized environment, the terms of a pension plan may be collectively negotiated, which may restrict an employer's ability to alter or amend the plan terms without union consent. This issue may need to be considered in a transaction where the existence of a collective agreement may affect the range of choices available to a vendor or purchaser concerning the treatment of benefit plans applicable to unionized employees.

A collective agreement may also require an employer to make contributions for unionized employees to a multi-employer pension plan or a multi-employer benefits plan that is not maintained or administered by the employer. Whether the employer has additional contribution obligations under such a plan, other than to make the contributions required under the collective agreement, may be an issue.

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Osler's Pensions & Benefits Department offers a dedicated team of lawyers with experience in every aspect of this complex, multi-jurisdictional area of the law. Jon Marin and Julien Ranger are both members of our department. Further information on Registered Pension Plan, proposed regulatory amendments and changes to pension investment rules can be accessed at our Pension and Benefits Law blog.