CAN YOU TAKE IT WITH YOU?

By Jennifer Paterson

In an age of work mobility, Canada's retirement savings system has some way to go in addressing the portability of people's pension savings

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The days of working for one employer and contributing to a single pension plan for an entire career are long over. In fact, 28 per cent of Canadians surveyed by Workopolis Inc. in 2014 had already had between five and 10 jobs, and Statistics Canada figures show defined benefit membership is continuing to fall while more people are contributing to defined contribution pensions and other types of savings plans.

The changes suggest most employees will have a number of retirement accounts throughout their working lives, as they leave employers and pension pots simultaneously. Does pension legislation make the transitions straightforward or are there gaps in pension portability?

Transferring defined benefit assets

The original defined benefit plans were paternalistic and designed as the ultimate employee retention tool. "Sometimes, they were alluded to as golden chains," says Bob Baldwin, an Ottawa-based pension consultant. "And it speaks to the point that, from the employer's perspective, the pension plan was a way of trying to chain the employee to the employer, as it were, so there wasn't a lot of interest in either short vesting periods or portability arrangements."

Today, when employees leave an employer and are more than 10 years from the normal retirement age, they can transfer the commuted value of their pension balance to one of the following three savings vehicles: another registered pension plan, if the administrator accepts such amounts; another registered retirement savings plan, such as a locked-in retirement account or a life income fund; or an insurance company for the purchase of an annuity, at the discretion of the plan they're leaving.

The options do make benefit accruals portable but they do so in a way that essentially transforms a defined benefit accumulation into a defined contribution one, says Baldwin. "There was some argument . . . that the preferable approach would have been to require the indexation of DB promises so that they would remain in a DB form, but that option never materialized."

Another consideration around the portability of defined benefit pensions is how much a plan member can transfer on a tax-deferred basis. There are a number of complicating factors, including the maximum transfer value limit under the Income Tax Act, notes Gavin Benjamin, a senior consultant and actuary with Willis Towers Watson's retirement practice.

"As a result of that, when you have more mature employees transferring their lump-sum value, quite often a significant portion of their entitlement is not tax-deferred."

The issue of tax limits

Indeed, the maximum transfer value limit is a potential barrier to pension portability that governments can address through changes to tax legislation, says Rosalind Gilbert, an associate partner in Aon Hewitt's retirement and investment consulting practice in Vancouver.

The limits are determined by multiplying the lifetime pension by a prescribed age-based value factor. They "were originally introduced by the federal Department of Finance to prevent DB plan members from receiving pensions higher than those they could accrue in the DB plan by transferring their benefits to RRSPs and deferring receipt of pension income," says Gilbert.

"If you look at maximum transfer values, I think there may be some merit in looking at how those have been impacted by the low interest rate environment," she adds, noting the prescribed factors date back to the early 1990s, when bond yields were more than 10 per cent. This summer, long-term Canadian bond yields were close to four per cent.

As a result, commuted values are often much higher than the maximum transfer value limit, notes Gilbert. She adds it would be difficult, if not impossible, for a defined benefit member who can only transfer a portion of the commuted value from the plan to create retirement income close to what would have been available from the plan. "Removing the [maximum transfer value] limits may allow members to defer receipt of pension income a bit longer but, since taxable income must be started from the recipient plan by age 71 at the latest, the government is unlikely to see much, if any, reduction in ultimate tax revenue as a result of such a change."

Potential changes to commuted-value transfers

The Canadian Institute of Actuaries appears to be on the same page. It's looking at a new standard for commuted-value transfers from defined benefit plans, particularly around the interest rates used to calculate those values. The current standard uses an interest rate linked to government of Canada bond yields, while the proposed change would base interest rates on a combination of provincial and corporate bond yields, says Benjamin.

While the implications of the proposal will depend on the relationship between provincial, corporate and government of Canada bond yields over time, Benjamin notes it could lead to a reduction in commuted values.

The other significant proposal for the standard relates to certain target-benefit and multi-employer plans with fixed contributions and for which legislation permits a reduction in accrued benefits if

EMPLOYEES ON THE MOVE

How many jobs have Canadians had?

1: 6%

2: 8%

3: 14%

4: 15%

5: 13%

5 to 10: 28%

More than 10: 6%

Source: Workopolis survey published in 2014

FIVE JOBS, FOUR RETIREMENT SAVINGS PLANS

Since 36-year-old Emily Edwards began working more than 10 years ago, she has had five different employers and been a member of four registered savings plans. With all of her job mobility, she's lucky those different pots aren't scattered all over Ontario.

Edwards' first full-time employer was the Toronto-based C.D. Howe Institute, which offered a group registered retirement savings plan with matched contributions. While departing employees could transfer the funds to another savings vehicle, Edwards used her RRSP for a down payment on her first home when she left the organization in 2009.

Her second employer, Trees Ontario, didn't offer any type of retirement savings arrangement. But her third employer, the Toronto Zoo, and the one after, the University of Ontario Institute of Technology, both automatically enrolled her into a defined contribution pension plan.

Each new employer also gave her the option of transferring any registered savings from her previous organization. "With the zoo and UOIT, I was able to move funds into my new pension," she says. "With UOIT, I had the option of leaving my funds with Sun Life, even though I was no longer employed with the university."

Earlier this year, she began a role at Queen's University, where she's contributing to yet another defined contribution plan. "I am able to bring all of my former pension savings with me into the new plan and I'm still in the process of doing this now," she says.

the financial performance of the plan is lower than expected, says Benjamin. "For those types of plans, what's being proposed is that commuted values would be calculated in quite a different way. For someone who leaves and elects for a commuted-value transfer, that person gets a share of the plan assets at the time they leave. So basically, you calculate the liability for the person who's leaving and you compare it to the total plan liabilities."

Multi-employer options, PRPPs and the Saskatchewan Pension Plan

Whether the Canadian Institute of Actuaries' proposals take effect or not, multi-employer pensions already have built-in portability. Their reciprocal transfer agreements are somewhat limited in scope, says Baldwin, noting each individual plan takes the initiative to create some degree of portability. "You have a similar pattern in the public sector where you've got networks of public sector plans that have reciprocal transfer agreements to facilitate movement from one plan to another by individual employees," he adds, noting that isn't often the case with single-employer plans.

Portability is also a feature of pooled registered pension plans, as they offer Canadians a registered arrangement not associated with only one employer, says Karen Tarbox, a senior retirement consultant at Willis Towers Watson.

The Saskatchewan Pension Plan, an arrangement introduced in 1986 to help Saskatchewan residents who didn't have a workplace pension, is often referred to as the working model of a PRPP, according to its general manager, Katherine Strutt. It's now available to all Canadian residents and has an annual contribution limit of $2,500, up from its original cap of $600.

Gilbert agrees that Saskatchewan's plan falls into the same bucket as PRPPs. "They basically allow individuals that don't have access to a workplace program already to put money aside for retirement within a more professionally managed program," she says. "Generally, the expectations are the fees are lower, there's oversight in the investments and that kind of thing."

And since the plan allows for transferring RRSP funds into accounts, the model could be a good solution to pension portability if combined with personal savings, Gilbert adds. But the issue around the Saskatchewan Pension Plan, as well as PRPPs, is that as voluntary programs, awareness and participations rates tend to be low, notes Baldwin. "It probably suggests that voluntary solutions to pension coverage problems may not be very effective."

Indeed, while the PRPP model is in place in most Canadian jurisdictions, it hasn't really taken off yet, says Tarbox. "It's still early days. Until something has been brought into force in the major provinces, it's never going to have traction. It's one solution. There's been lots of discussion and debate about that in the last five years. We'll see how it plays out in the market."

Defined contribution plans, RRSPs and other savings options

While plan members face tax issues when transferring amounts out of a defined benefit pension, moving funds from capital accumulation plans is much simpler. "So DC to DC or group RRSP to DC, the money is already in a tax-sheltered environment, so you don't have to have extra RRSP room to enable a transfer; it can just be a direct transfer," says Gilbert.

Depending on the plan design, however, there could be added administrative complexity, says Tarbox. "Sometimes, they'll accept locked-in funds but they don't want to have any non-locked-in funds, because the plan doesn't provide for other additional voluntary contributions or foresee any situation where funds have been non-locked in."

The main issue is whether the new employer is willing to accept the transfer. The former employer must offer a transfer to the departing member, but there's no legislation requiring the new organization to accept it. Is it time to legislate such a requirement?

Tarbox believes the framework for pension portability is already in place and further legislation is therefore not necessary. "We have natural fragmentation in the market in Canada because plans are voluntary and we have a range of designs," she says. "I don't know if you can make portability any easier than it is, given the nature of the plans and the retirement system we have in Canada."

But due to an increasingly mobile workforce, Bita Jenab, a principal at RetirementWorks Services Inc., believes employees are looking for ways to consolidate the retirement benefits they earn from multiple employers and suggests there's a role for the industry to play. "The industry needs to respond to this workforce reality by improving portability of capital accumulation plans," she says.

"CAP sponsors can set up their plans to accept funds transferred from other CAP plans. Employers in a specific industry can band together to offer reciprocal agreements, similar to what is available in the public sector, and the pension regulators can support this by legislating that CAP plans not only offer portability out of a plan but also accept funds transferred from another CAP plan."

It's also important to help plan sponsors understand the value of enabling transfers, says Gilbert. "I think that would be more on the grounds of, the more money they have in their plan, potentially the lower fees they'd have. It's hard to see a reason to prevent transfers into a DC program."

But Doug Andrews, an adjunct professor of statistics and actuarial science at the University of Waterloo, can see why the new employer may not want to accept a transfer.

"On the one hand, it's more work for the employer that's accepting funds. And the funds that come may be subject to locking-in rules, and so on, that have to be traced."

Benjamin has seen a different viewpoint among some of his U.S. employer clients, which encourage employees to stay in the plan since it offers lower fees than in a retail environment. "So their viewpoint is more, we actually encourage our former employees, for their own good, to keep the money in the plan."

It's understandable why many plan members would find it challenging to leave the comfort of a group savings product behind and go out into the world of retail pricing. The Saskatchewan Pension Plan, for instance, targets a low expense ratio of one per cent or less, so members have the advantage of institutional pricing, says Strutt.

Most insurance companies also offer an option that provides a stepping stone between a group and a retail program that employees can move into when they leave an employer. Particularly relevant for employees leaving a defined contribution plan or a group RRSP, they have the choice of transferring their money into a product that looks like a group option but isn't through a specific employer, notes Gilbert.

"What it gives employees is a sense of familiarity," she says. "They've been used to using an insurance company's online system for accessing their funds and looking at their investments, so all of that is very familiar and a lot of the tools and resources are the same. It provides a little more comfort than just booting them out into the world of individual retail."

But the issue isn't having those options available to departing pension members; it's making sure they understand the change. Gilbert warns that employers must make sure the member knows they're no longer overseeing the plan. Also, there's usually a much broader menu of investment choices than members would have had through their workplace plan, so they must be aware of their new responsibilities. "In a different situation where they're either not employed or moving towards retirement, they have to think about different things," says Gilbert.

And employees may not realize they're facing higher fees when moving their savings from their workplace plan, an area where Andrews would like to see legislation introduced.

"The monies that are there are pension monies, so why shouldn't pension monies always be entitled to have lower fees attached to them? I don't know how receptive politicians are to making changes in this area . . . but I think that's definitely one area where legislation is important."

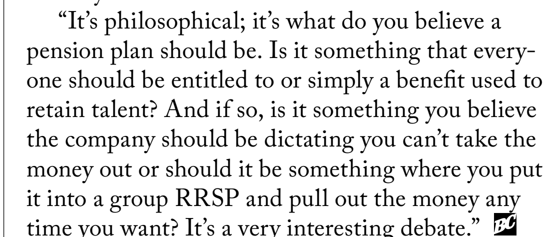
Time to unlock?

If governments are going to make legislative changes, they should probably start with the maximum value transfer limits, says Benjamin.

"I haven't heard an indication that the federal government is interested in addressing that limit but I think in terms of creating barriers to portability, I see that as something that, in an ideal world, would be addressed."

For Mitch Frazer, a pension lawyer at Torys LLP, the issue isn't with portability but with unlocking. "So the big debate is whether people should have the ability to unlock [and] how portable should it be? I don't think there's a big concern, in terms of portability. . . . It's not a black or white topic. There are benefits and drawbacks to whatever course of action you take.

"It's philosophical; it's what do you believe a pension plan should be. Is it something that everyone should be entitled to or simply a benefit used to retain talent? And if so, is it something you believe the company should be dictating you can't take the money out or should it be something where you put it into a group RRSP and pull out the money any time you want? It's a very interesting debate."



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THE SASKATCHEWAN PENSION PLAN IN NUMBERS

1986
Plan introduced

$600
Annual contribution cap when the plan began; the government matched up to $300 for low-income contributors

1992
Government match discontinued

$2,500
Current annual contribution cap

33,000
Approximate number of members in 2016

20%
Approximate percentage of members who live outside Saskatchewan

$450 million
Plan's assets in 2016

21
Plan's ranking on *Benefits Canada*'s 2017 list of the top 50 DC plans

Source: Saskatchewan Pension Plan