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Highlights

While amendments to the PBA and FLA contained in Bill 133 simplify the rules in Ontario surrounding pension divisions on marriage breakdown, critics argue they could prove unfair to spouses. In addition, pension plan administrators will have to assume the new role of valuing pensions for family law purposes. However, the old rules will continue to apply in certain situations, thus further complicating the role of administrators.

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Are You Prepared for New Pension Splitting Rules? What You Should Know About Ontario's Bill 133

Despite their frequency, pension divisions on marriage breakdown can raise many difficult questions. Pensions often amount to a significant portion of a family's assets, and some separating spouses must share accrued pension benefits to equitably divide their property. In addition, pension divisions are complex, with the options for how and when to split a pension depending on the particular plan, jurisdiction and member circumstances.

Now Bill 133, the *Family Law Statutes Amendment Act, 2008*, will transform Ontario's rules in this area. The Bill, which received Royal Assent on May 14, 2009, amends the *Family Law Act* (FLA) and the *Pension Benefits Act* (PBA), and includes significant changes to the manner in which pensions can be valued and divided following a marriage breakdown. Once the regulations are drafted and the pension rules are proclaimed in force (which is not expected until at least the end of this year), extra caution will be needed in shifting to the new rules. But looking further ahead, it should be easier for plan members, spouses, family lawyers and plan administrators to maneuver through this new regime.

A "Clean Break" for Separating Spouses

Under current Ontario rules, it is rarely possible to transfer a share of a member's pension to a former spouse at the time of separation. Spouses who use a pension to divide their net family property must usually resort to "if and when" arrangements, where the member's pension cannot actually be split until the member terminates employment, dies or retires. This method is widely criticized because the property division may not happen for many years.

Ontario is unlike other provinces in that a former spouse's payments from a pension plan are linked to the member's pension payments. Under an "if and when" arrangement, monthly pension payments being divided at source between the member and former spouse would cease with the member's death. If the member dies shortly after retirement, the former spouse might receive far less from the pension than expected. In British Columbia, Nova Scotia and Newfoundland and Labrador, pension divisions are generally delayed until the members' pension comes into pay; however, in these provinces, former spouses can receive a separate pension from the plan that is not dependent on the member's life.

Bill 133 introduces a new PBA section to allow a former spouse of a plan member who has not retired to apply for an immediate lump sum transfer of his or her entitlement out of the plan. This will make Ontario more comparable to Alberta, Saskatchewan, Manitoba, Quebec, New Brunswick and the territories where immediate settlements of pension divisions are permitted.

Lump sum transfers under this new regime must generally be locked-in. Pension plans can also specifically allow a former spouse to keep his or her share of the member's pension in the plan's fund. New regulations will have to provide guidance regarding the obligations a plan administrator would have towards a former spouse whose pension assets remain in the fund.

For retirees, the Bill allows pension installments to be split but the lump sum transfer is not an option. If the plan permits, a former spouse of a retiree can also apply to the administrator for a single pension that would replace the pension split and any entitlement to a joint and survivor pension that the former spouse may have. Another option for the former spouse is to waive the joint and survivor pension, presumably in favour of an increase in value elsewhere.

Streamlined Valuations

Many are applauding the changes which will streamline pension valuations for marriage breakdown purposes, but some experts warn that the new rules oversimplify pension realities, and may lead to inequities. Currently, the process works as follows.

To determine the net family property to be divided between spouses, parties usually hire an actuary to estimate a range of values for the member's pension based on several different scenarios, and taking into account basic vested pension rights at the date of separation as well as additional non-vested benefits such as early retirement rights and non-guaranteed indexing. The parties or a judge use those values to arrive at an estimated value for the pension that seems most appropriate for the particular case.

If the parties ultimately decide to use the pension to divide net family property and the plan is asked to make payments to a former spouse for this purpose, the plan administrator must re-calculate the value of the vested benefits at that time based on assumptions which may be different than those used for net family property purposes and ensure that no more than 50 per cent of the pension that accrued during the marriage is paid to the former spouse.

This means two different calculations are performed, often at very different times, and the amounts may not be consistent.

Under the new rules, spouses can request a pension valuation from the plan administrator when they are negotiating their net family property (rather than hiring an actuary). The administrator will calculate a “preliminary value”, which is the value of the member’s pension at the family law valuation date. It is likely the preliminary value will be calculated as though the member terminated employment at that date. It will not include most increases or other improvements that could arise after the date of separation, but may include adjustments for ancillary benefits and other entitlements. Details of these calculations will be set out in the regulations.

The administrator will then use a prescribed method to calculate the “imputed value for family law purposes”, which is the portion of the preliminary value that can be attributed to the marriage, and provide this amount to the member or spouse. The amount or proportion of the imputed value that is to be paid to the spouse must be set out in the divorce order, arbitration award or domestic contract. The plan administrator will not have to recalculate the values if an application is later made for a lump sum transfer to the former spouse.

This new method is simpler but critics warn that it also means net family property could potentially be undervalued and former spouses could be short-changed. It captures the value of the pension at a particular point in time – a method that could be unfair to the former spouse if this snapshot ignores future events that are likely to increase the value of the member’s pension. Until the regulations are drafted, we are reserving judgment about the effectiveness of these valuation provisions.

Pensions Outside of the PBA

Bill 133 excludes Canada Pension Plan (CPP) credits from net family law property under the FLA. There is already a federal government system in place for applications to divide CPP credits on marriage breakdown. Excluding CPP credits from net family property divisions under the FLA ensures that divorce orders and domestic contracts will not contain terms that conflict with the federal CPP credit division provisions.

Other pension plans that are not subject to the PBA are included for division purposes under the FLA. The new PBA valuation rules are to be applied to these other pension plans where reasonably possible and with necessary modifications.

Hewitt Comment

Getting from Here to There
The transition from current to new rules may cause confusion. All court orders, awards and domestic contracts that are made before the new legislation is in force must be addressed using the current rules, even if the member is far from retirement. Plan administrators will have to pay close attention to the dates that documents are created (rather than when they are filed).

Court orders and domestic contracts that were made under the current rules, but amended after the new rules come into force, may continue to be governed under the current rules. This will require that pension plans continue administering monthly pension payments under the "if and when" approach for an indefinite period of time. Plan administrators will therefore need to determine the nature and purpose of these amendments to judge which rules apply.

Prepare Now for Changes

Although the new pension provisions are not yet in force and the regulations are still forthcoming, pension plan administrators and employers should start preparing for the new system now, and should speak to their third party service providers about this issue. In most cases, preparation will include the following steps:

- *Review administrative processes to determine what needs to be done to reflect the new rules. Administrators will now be responsible for valuing pensions for family law purposes, a task that is currently performed by actuaries hired by members and former spouses. Who within the administrator's team will perform this function for your plan?*

- *Consider member communication strategies. How and when should plan members be advised of the new rules?*

- *Develop an understanding of what information and documentation you will need from the parties in order to proceed with the prescribed valuations and credit splits. Will you need new forms and processes to capture information that has not been captured in the past?*

- *Think about whether a fee will be imposed on the party making the application for the valuation, as permitted by the Bill (details of which will be included in the regulations).*

- *Determine whether the pension plan's current terms match the new rules and provide sufficient authority and protection for the administrator's duties and responsibilities under the new legislation. Are lump sum transfers to former spouses permitted under the current wording of the plan text? Will it allow for the spouses' portions to be maintained in the plan? Amendments may be required.*

Members, former spouses and their advisors will want to take note and determine whether or not a pension credit split (or an amendment to an existing one) should be delayed until the new rules are in force. Going forward, these parties will want to consider the extent to which an independent actuary should be hired for advice, since there may still be a role for them under the new system.

While family lawyers try to achieve a clean break for their separating clients, Ontario's current pension laws often prevent this from happening. Although the amendments contained in Bill 133 are not perfect, they appear to be moving in the right direction – towards a simpler and more accessible regime and one that is more consistent with the *rules in other Canadian jurisdictions. However, while former spouses will have new options that provide them with greater independence under the amended valuation provisions, the new rules may negatively impact their financial interests. It remains to be seen whether the regulations, when finalized, will safeguard those interests.*

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