COUGHLIN
employee benefits specialists

COURIER

SEPTEMBER 2009

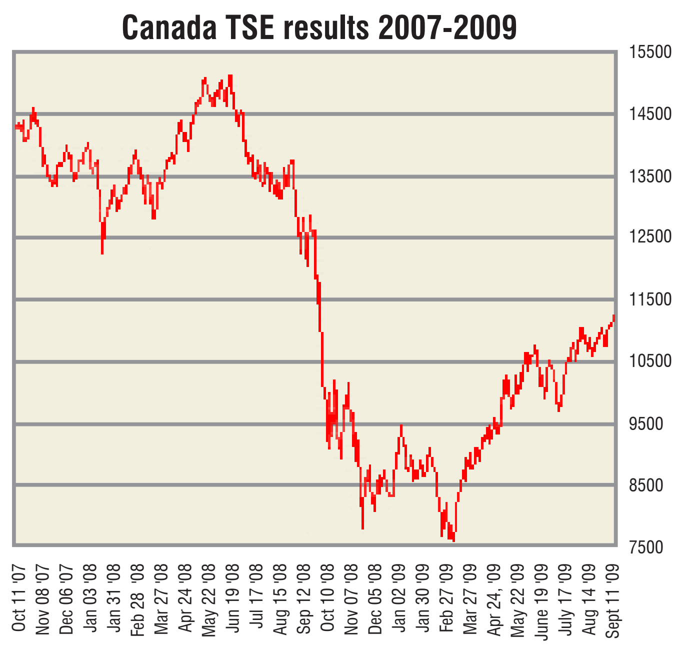
AT A GLANCE ...

Optimism shines as pensions dig out from market storm

Like a city after a two-foot snowfall, pension fund managers, plan sponsors and members are now surveying the damage from the 2008-09 market crash and recession, and are beginning to dig out from the sharpest economic downtown since the 1930s.

From a high of 14,500 points in May 2008, the Toronto Stock Exchange collapsed to a low of just 7,500 at the market's ebb in March 2009, wiping out billions of dollars in pension values in Canada alone. Worldwide, more than $1.5 trillion has been erased from the assets of the world's 300 largest pension funds, according to a Watson Wyatt study.

However, despite the blizzard of bad news of bank failures and bailouts in the US, along with plant closings and a loss of confidence in the lending markets, the world economy realized a record bounce, due largely to emergency funding by governments everywhere. From its March 2009 low, the TSE sprinted past the 11,000 mark in September, signalling that the worst could be over.



From its May 2008 high of 14,500, the Toronto Stock Exchange collapsed to 7,500 in March 2009 only to recover to touch the 11,000 level in September 2009.

Reflecting the market bounce, asset values of Canadian pension plans grew by 9.5 per cent from April to June 2009, according to RBC Dexia Investor Services.

"Given last year's brutal pull-back, plan sponsors are breathing a sigh of relief to be finally moving into positive territory, especially after the poor start in January and February," says Don McDougall, RBC Dexia's director of advisory services.

With the recovery comes optimism. According to a Watson Wyatt survey of 439 finance executives in Canada, the US and the UK, 86 per cent feel that they have enough cash to fund their pension plans for the next two years, despite the fact that 87 per cent reported that their plans' financial strength had been negatively affected by the market meltdown.

The optimistic tone varies considerably from late 2008 when a separate study of Canadian, American and European executives by SEI Investments reported that

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New consultant joins Coughlin

President Brian Bockstael is pleased to announce the appointment of **Jim Robinson** as senior consultant.

Mr. Robinson joins Coughlin following an extensive career in group insurance and employee benefits consulting.

He began his career in 1967 as a group insurance representative and later, office manager, with Aetna Canada. In 1976, he joined Towers Perrin, a national employee benefits and pensions consultant. He was associated with that organization, including seven years as a principal of the firm, until 1990, when he returned to Aetna as its vice-president of marketing.

From 1992 to 1998, Mr. Robinson was vice-president of Canadian operations for The Segal Company, a US-based actuarial and consulting firm specializing in providing benefits to multi-employer trust funds and public sector organizations.

In 1998, he joined Sedgwick Noble Lowndes Montreal, a UK-based pension consultancy and financial advisor. He was managing executive there until its acquisition by Mercer, the world's largest human resources consulting firm. He was associated with Mercer's Ottawa organization as a principal until 2002, when he joined Sun Life's Ottawa group organization as an account executive.

As senior consultant, Mr. Robinson will be responsible for servicing and advising Coughlin clients in the Ottawa and Toronto areas. He will also act as a resource to Coughlin's benefits consulting team. ❧

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two-thirds of plan sponsors had either made or were planning to make changes to their plans' asset allocation strategies to try to preserve their pensions' values.

Canadian defined benefit pension plan sponsors were the most diverse in their assessment of the turmoil experienced in the past year. A total of 87 per cent of Canadian defined benefit plan managers surveyed by Towers Perrin said their organizations' pension plans were negatively impacted by the downturn. This compared to 67 per cent in the US and 49 per cent in the UK. Despite that, Canadians were also the most positive of those surveyed, with 71 per cent of respondents expressing optimism about their pensions' long-term viability, saying they were focusing on long-term strategies designed to reduce the risk levels within their pension portfolios.

Similar results were reported by SEI Investments, which reported that only 20 per cent of Canadian executives feel that the market's volatility has increased their likelihood of terminating their pension plans in the near future, compared to 46 per cent in the US. That optimism is also expressed in new member enrolments, with 70 per cent of Canadian pension plans being open to new enrolments compared to 55 per cent in the US, the SEI study said.

It appears that Canadians generally have been most accepting of the *"new retirement reality"*, according to Towers Perrin, with 87 per cent of executives saying that the 2008-09 market downturn has caused *"a long-term shift in how companies and workers prepare for retirement,"* compared to 72 per cent of US respondents and 37 per cent of those in the UK. Part of the "new reality" includes the postponing of retirement plans by workers and a greater appreciation of the value of defined benefit plans by both plan members and plan sponsors.

Next question: Will the appreciation for more conservative pension asset allocation strategies be maintained or, will the bitter lessons of the 2008-09 market crash be forgotten as the recovery continues? ❧

Recession sparks drop in drug sales

Canadians are spending less on prescription drugs since the start of the recession, according to a study released by Brogan, a Canadian health care research firm. In its report entitled *"From Wall Street to the pill cabinet"*, the group says that there was "a rapid drop" in prescription drug sales over the two fiscal quarters following the start of the recession.

Leading the decline are sales of anti-thrombotic drugs used to reduce blood clotting.

While the study admits that *"the relationships between slowing private sector drug sales and the employment situation is unclear,"* an earlier *Emerging Trends* study by Morneau Sobeco suggested that a drop in drug claims during economic uncertainty is often a result of patients either drastically reducing or foregoing their drug treatments altogether. Ultimately, it leads to a spike in hospitalization and disability claims later on. (See the July 2009 edition of the *Coughlin Courier* for background.)

If true, watch for a jump in hospitalizations and disabilities, particularly in the communities and workplaces hardest hit by the recession. ❧

Joint BC-Alberta provincial pension plan receives mixed reviews

A plan to provide national pension coverage for workers that do not have a workplace pension plan received a mixed response from provincial premiers this past summer.

Responding to a joint British Columbia-Alberta plan to offer voluntary defined contribution pensions to workers in addition to Canada Pension Plan (CPP) coverage, provincial leaders of Ontario, Manitoba and Nova Scotia agreed to join British Columbia and Alberta to launch a formal review to improve the retirement income of Canadians.

Only 25 per cent of private sector workers in Canada had a workplace pension plan in 2005, down from 35 per cent in the 1970s, according to data published by Statistics Canada. Plus, with the solvency of corporate pensions battered by stock market declines and corporate failures, governments across the country are now realizing that many Canadians will have little or no pension income at retirement outside of the government-based Canadian Pension Plan and Old Age Security benefits. With the bulk of the baby boom generation on the edge of retirement, governments could face a pension income crisis within the next 10 years if additional retirement savings are not generated.

While Ontario didn't reject the joint BC-Alberta plan, the nation's largest province argued that a broader range of pension options should be studied before a parallel plan to the CPP is introduced nationwide.

"We're in agreement that governments at all levels have to look at this and begin to look at options available to ensure that we continue to have a retirement income system that is adequate for all Canadians," says Ontario Finance Minister Dwight Duncan.

Complicating the situation are issues such as interprovincial labour mobility, the role of private sector retirement savings vehicles such as registered retirement savings plans (RRSPs) and tax-free savings accounts (TFSAs) in retirement planning, and Canada's fragmented financial regulatory system.

While the possibility of a new government pension plan has generated some interest at the provincial level, the insurance industry and some consumer groups question the need for yet another government-based pension plan. Rather than developing a third government pension scheme, the provinces should focus on harmonizing Canada's patchwork of pension regulations, they argue.

"Some of the proposals relate to a government sponsored defined contribution plan, and we don't think that's the best way to go," says Canadian Life and Health Insurance Association (CLHIA) President Frank Swedlove. *"We think there are opportunities to increase pension activity by changing some of the pension rules that already exist in the country."*

Mr. Swedlove's comments were mirrored by Sun Life President Donald Stewart who suggested that the Income Tax Act and other regulations be amended to better allow smaller companies to participate in pensions through multi-employer arrangements or similar "umbrella" plans.

"Life insurers want a major overhaul of federal and provincial pension laws in general. These laws were written in an era of defined benefit plans and have not been properly updated following the dramatic shift toward defined contribution plans," the CLHIA President says.

Another idea tabled by the insurance industry includes limiting personal RRSP contributions to a lifetime maximum, rather than annually. This will encourage people to increase their retirement savings contributions later in life, when they have more disposable income.

While the BC-Alberta plan may not survive scrutiny by the various provinces, British Columbia Finance Minister Colin Hansen and Alberta Finance Minister Iris Evans have pledged to work together to develop a dual-provincial pension plan even if their plan is not accepted at a national level.

"We have a serious savings problem in this country," says Scott Sweetman, co-chair of the BC-Alberta pension task force. "*That's the bigger message that needs to get across. People are just not saving enough. My advice to our ministers is to keep going. If you want to do something nationally, terrific. But we don't need to wait for it."* ❧

Supreme Court rules on pension expenses and surpluses

The Supreme Court of Canada has upheld lower court rulings allowing pension plan sponsors to use pension assets to pay for plan expenses and to take pension contribution holidays.

The ruling put a final end to a decades-long dispute involving the members of the defined benefit plan administered by Kerry Canada Inc.

The case involves a defined benefit (DB) plan established by the company in 1954. In the 1970s, the plan was amended to allow its expenses to be paid from the plan. While the plan sponsor paid all plan expenses from 1954 to 1984, it began taking contribution holidays in 1985. In 2000, the plan was amended to allow it to include a defined contribution (DC) component. The plan sponsor then began to use the surplus generated by the old defined benefit pension to make contributions to the defined contribution portion of the plan. The plan members objected and raised the issue with the Superintendent of Financial Institutions. (See the August 2007 edition of the *Coughlin Courier* for background.)

The Superintendent initially ruled in favour of the plan members. However, through a series of appeals, the case was reviewed by the Ontario Divisional Court and the Ontario Court of Appeal, both of which generally sided with the plan sponsor.

The final ruling of the Supreme Court covered four broad areas. They were:

1. Plan expenses. The Court rejected members' arguments that plan expenses should never be paid from the pension fund since payments were not made for the *"exclusive benefit"* of the members. In its ruling, the Supreme Court noted that payment of expenses is necessary to *"ensure the integrity and existence of the plan."* Since the continued existence of the plan does benefit all plan members, it was considered reasonable that the plan's trust fund pay for the bona fide expenses related to the pension plan, regardless of who provided the eligible services.

2. Contribution holidays. The Court ruled that when pension funding is backed by actuarial practice, plan sponsors may take contribution holidays, unless their plan document says otherwise. Since the Kerry pension did not prohibit the practice and the appropriate funding was in place, the plan sponsor had a right to take contribution holidays.

3. Using surplus from a DB plan to fund DC contributions. Since both the defined benefit and defined contribution elements of the plan functioned under one trust fund, applying assets from one of the plan's components to support the second component did not violate or revoke the trust agreement, the Court said. Since neither the pension plan nor the trust fund were terminated when the surplus was used, and since the plan's funds were not withdrawn or misused, the interests of the members of the defined benefit plan were not violated, the Court ruled.

4. Costs. The Supreme Court agreed with lower court rulings that said members' litigation costs could not be paid from the pension fund, given both the adversarial nature of the litigation and the fact that the litigation itself *"was not advanced for the benefit of all plan members."*

For plan sponsors, the Kerry ruling provides both clarity and closure on a contentious issue: plan funds *can* be used to pay expenses, provided the expenses are *"reasonable"*, relate directly to the plan's administration and are not misused. As well, assets from older defined benefit plans *can* be used to support newer defined contribution elements of the same pension plan. ❧

Collaborative treatment can reduce STD costs

Plan members on disability from mental illness return to work sooner when their family doctor and mental health professionals actively work together, according to a study released by the Centre for Addiction and Mental Health (CAMH).

According to the study's author, Dr. Carolyn Dewa, 85 per cent of short-term disability claimants studied by the CAMH were able to return to work when family doctors, psychiatrists and other mental health professionals collaborated in their treatment programs, compared to 63 per cent who relied solely on standard psychiatric care and 31 per cent who relied only on their family doctor for their therapy.

The study, which was published in the July 2009 edition of the *Canadian Journal of Psychiatry,* estimates that the collaborative approach can save employers an average of $503 per patient in short-term disability claims and related costs.

Fragmentation of medical treatments can often result in delays and less effective rehabilitation and follow-up, the study suggests. With up to 10 per cent of the working population diagnosed with depression and other mental illnesses each year, the cost savings of the collaborative treatment approach could amount to $17 billion for the economy, according to the CAMH.

"Our findings demonstrate that partnering or collaborative care is more cost-effective, increasing the number of people who are able to return to work while decreasing the number of people transitioning to long-term disability," Dr. Dewa says. *"The cost of mental illness is a large burden on the economy, but if we are able to find new ways to work together, we can provide better care and decrease those losses."* ❧

Federal pensions lose $5.1 billion

The Public Sector Pension Investment Board, the agency responsible for the federal public service pension plan, announced it lost $5.1 billion from March 2008 to March 2009, a 23 per cent decline.

Equities led the plan's portfolio decline, experiencing a 30 per cent loss from a year ago. The value of its real estate holdings dropped by 17 per cent over the same period while its bond portfolio declined by 19 per cent.

In addition to the federal public service, the organization also manages the pension assets of the Royal Canadian Mounted Police, the Canadian Forces and the Canadian Reserve Force. ❧

Ontario and BC to join Harmonized Sales Tax

Ontario and British Columbia will join Newfoundland, New Brunswick and Nova Scotia in harmonizing their provincial sales taxes with the federal Goods and Services Tax (GST), beginning July 1, 2010.

With the new Harmonized Sales Tax (HST), the provincial sales tax will be merged with the GST to create one single tax on most transactions. In Ontario's case, it will mean its eight per cent provincial sales tax (PST) will be combined with the five per cent GST to create a tax of 13 per cent. In British Columbia, which has a PST of seven per cent, the rate will be 12 per cent.

The HST is collected by the Canada Revenue Agency, which then remits the appropriate amounts to the participating provinces. Supporters of the tax argue that consolidating federal and provincial tax collection will save money and promote greater tax fairness as tax attribution will shift to the point of transaction, rather than only the point of sale.

Opponents say the tax will add to costs and inflation as an item may be taxed at several stages of its production process before it is sold as a finished product or service to its ultimate consumer. As well, previously exempt services such as benefits and pension consulting services, insurance premiums, mutual fund fees, pension fees, accounting fees, funeral services, internet services, and other services that previously were PST-exempt will be subject to taxation. In this sense, the HST is similar to the value-added tax (VAT) used in most European countries.

The provinces of Manitoba and Quebec are also considering joining the HST program.

The impact of the new HST on Coughlin's services will be conveyed to our clients when specific details are confirmed. ❧

CPP assets rise by $11 billion

The Canada Pension Plan (CPP) Investment Board reports that the CPP fund rose by $11.1 billion in the first quarter ending June 30, 2009. Plan assets totalled $116.6 billion compared to $105.5 billion at the end of March 2009. ❧

Caisse writes off $5.7 billion

The Caisse de dépôt et placement du Québec has announced that it will write-off more than $5.7 billion for the first half of 2009, effectively wiping out any investment gains recorded so far this year.

The pension fund manager says risky loans, particularly second and third mortgages in the US commercial real estate market, and other risky investment strategies are responsible for the unexpected losses.

The Caisse recorded a five per cent return on its other investments as of June 30, 2009.

The organization, which manages 25 provincial pension plans, including the Quebec Pension Plan (QPP), invested heavily in higher risk commercial property ventures that generated higher interest rates and returns for many years. However, the Caisse's strategy unravelled in 2008 when the US property market collapsed. It lost more than $40 billion last year, a return of -25 per cent. The median loss recorded by Canadian pension funds was 17 per cent in 2008.

Chief Executive Officer Michael Sabia says the Quebec-based pension fund manager will no longer invest in higher risk "mezzanine" loans or other forms of subordinate real estate loans.

The Caisse de dépôt et placement du Québec is Canada's largest pension fund manager."❧

Quebec tax increase

The Quebec government has announced that it will increase its sales tax on goods and services to 8.5 per cent from the current level of 7.5 per cent, beginning January 1, 2011. The tax will apply to ASO and other services.❧

RAMQ changes

Effective July 1, 2009, the maximum premium for Quebec employees and retirees insured by the Régie de l'assurance maladie du Québec (RAMQ) will increase to $585 per year from $570.

As well, the co-insurance for RAMQ drug coverage will be reduced to 68 per cent, from 69 per cent.

The maximum annual contribution for private group plans was increased to $954 annually from $927.❧

Régie calls for QPP contribution increases

Contributions to the Quebec Pension Plan (QPP) could increase as early as 2011, according to the Régie des rentes du Québec.

In a working paper released this past June, the administrator of the Quebec public pension plan suggests that joint employee-employer contributions should increase to 10.4 per cent of pensionable income from today's level of 9.9 per cent.

In an attempt to address a projected funding shortfall that could exhaust the plan by 2051 (see the April 2008 and August 2007 editions of the *Coughlin Courier* for background), the working paper proposes increasing plan contributions by 0.1 per cent annually starting in 2011. If approved, plan sponsors and members should expect to experience QPP contribution hikes at that time.

The contribution increases would not apply to the Canada Pension Plan.

It has enough reserves to remain viable well past 2075, according to CPP Chief Actuary Jean-Claude Ménard.

Other proposed changes to the QPP include the following:

- tripling the orphan's benefit from $60 per month to $209 per month;
- tightening the QPP's disability pension requirements;
- changing the surviving spouse's pension from a lifetime benefit to a temporary benefit providing 60 per cent of the deceased spouse's unadjusted pension for a 10-year period; and
- reimbursing up to $2,500 of member contributions in cases when a plan member dies without leaving any direction on which family member should be entitled to receive the $2,500 QPP death benefit.❧

Who is the employer in MEPs plans?

When is an employer not an employer?

While that question may seem academic, it was the focus of the Financial Services Tribunal recently as it attempted to grapple with the implications of what the term *"employer"* means in cases of multi-employer plans. At stake were pension liabilities of a prominent national nursing association.

The case involved a national organization providing private duty nursing care in patients' homes. Under its original structure, each of the organization's local branches was established as a separate not-for-profit corporation, with salaries and other compensation controlled by the local branch. However, when it came to the management of its pension plan, the plan was never considered to be a multi-employer plan by its participants.

In 2006, the national organization attempted to consolidate the nursing agency's operations into a single organization. Local branches that did not accept the strategy were expected to disassociate themselves from the national entity.

While a number of the local branches chose to separate from the national entity, four branches declared themselves insolvent and partial wind-ups of the pension plans of the four branches began. It was then that the national organization declared the four branches would be responsible for funding any pension shortfalls arising from the partial wind-up of their portion of the pension plan. The local branches disagreed, stating that as the employer, the national organization should be responsible for any pension liabilities.

The case was passed to the Superintendent of Financial Services and, later the Financial Services Tribunal, the independent, adjudicative body with exclusive jurisdiction to settle all questions or appeals of decisions made by the Superintendent of the Financial Services Commission of Ontario (FSCO).

Ultimately, the Tribunal had to define the term *"employer"* under the province's Pensions Benefits Act (PBA), and with it, establish who would assume the liabilities for the four defunct branches. It had three possibilities to consider. They were:

- the employer was the one and only *"controlling employer"* of the plan; or
- the employer was *all participating employers jointly and severally,* regardless of their legal status; or
- the employer was the *person or organization that pays remuneration to employees.*

While the Superintendent, the branches and the organization's unions favoured the first definition, or, as an alternative, the second, the Tribunal ruled that the third definition most conformed to the Ontario Pensions Benefit Act.

"The PBA contains a clear and unambiguous definition of employer. That is the definition that should be applied," the Tribunal ruled. *"The only relevant factor in deciding who is an employer is which organization paid remuneration to the members who were branch employees."*

As a result, each of the nursing organization's branches was considered to be responsible for the pension obligations of its own employees while the national organization was responsible only for the pensions of the members that it directly employed.

Plan sponsors of either multi-employer pension plans or single employer plans with a number of participating employers should take note of the Tribunal's ruling, especially now when so many pension plans face solvency deficits. ❧

Fast facts

- Effective April 1, 2009, the Alberta health care plan will cover the prescription drug costs of individuals with rare genetic disorders. Under the program, the term *rare genetic disorders* is defined as medical disorders that affect fewer than one in 50,000 Canadians. It includes Fabry's disease, Gaucher's disease, Hunter disease, Pompe disease and MPS-I (Hurler/Hurler Scheie). Drug costs for these illnesses range from $250,000 to $1 million per year.
- The province of British Columbia has amended its health care regulations to allow licensed naturopathic physicians to prescribe drugs. There are more than 300 naturopathic physicians in the province. The province also now allows licensed optometrists to prescribe, dispense and administer prescription medications.
- British Columbia has also announced that it will increase premiums for its public health care plan by six per cent beginning January 1, 2010. Beginning in 2011, the province plans to peg premium rate increases to the annual recorded increase in health care costs.
- Newfoundland and Labrador has passed legislation allowing pharmacists to dispense medications prescribed by licensed practitioners in other Canadian provinces. The legislation will allow Newfoundlanders who work in Alberta, Ontario and other provinces but still have a residence in Newfoundland to fill out-of-province drug prescriptions when they return home.
- The co-payment for the Nova Scotia *Seniors Pharmacare Program* has been reduced from 33 per cent to 30 per cent.
- Ontario has introduced legislation to allow pharmacists to dispense prescription drugs without being physically present at the dispensing location. The new rules are designed to allow pharmacies in remote areas to dispense drugs under the supervision of a licensed pharmacist without the pharmacist having to be present at the time.
- The New Brunswick government says it will not appeal a Court of Queen's Bench ruling extending group health benefits to casual workers employed by the government. The ruling affects 7,600 government employees.
- The lifetime risk of contracting melanoma, according to the Canadian Dermatology Association: For men: one in 74; for women: one in 90. The lifetime risk of contracting melanoma in the 1930s: one in 1,500.
- Number of Canadians expected to be diagnosed with non-malignant skin cancer this year: 75,000. Number of Canadians who will learn they have malignant melanoma: 5,000.
- Approximately two per cent of women and four per cent of men have obstructive sleep apnea. ❧

PPN update

- The **Medical Arts Dispensary of Ottawa**, located at 160 Elgin Street in Ottawa, has joined the Coughlin & Associates Ltd. Preferred Provider Network. Their phone number is: 613-232-4851.
- The **Good Health Pharmacy** of 2-4188 Spratt Road in Gloucester has joined the Coughlin PPN. They can be reached at 613-822-8669.
- The former Bells Corners Pharmacy, of 62 Robertson Road in Bells Corners, is now a **Rexall Pharmacy**. Their phone number is unchanged at 613-820-4980. ❧

The Coughlin Courier is published by Coughlin & Associates Ltd.

Board of directors: Brian Bockstael, Kirby Watson, Mark Hogan, Brent Moore & Ken Kaitola

Editor: David Whitbread **Graphic designer:** Victor Lima

printed on 100% post-consumer recycled paper