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B.C. Re-thinks Pension Division Legislation

By: Thomas G. Anderson

In 2003, the Canadian Institute of Actuaries established a task force that reviewed Canadian **pension division law** and recommended model **legislation**, urging Canadian jurisdictions to adopt a uniform approach. In 2003, Alberta Finance reviewed the operation of the **pension division legislation** that had been enacted in 2000. Many jurisdictions (most notably, Saskatchewan) have recently made substantial changes to their **pension legislation** that affects matrimonial disputes (from extending the basic rules to include common **law** partners to fundamentally revising when and how **benefits** can be accessed). The Ontario bar is also deeply involved in developing recommendations to government for the implementation of modern **pension division legislation**. The latest effort is taking place in British Columbia where the province is currently reviewing its Family Relations Act.

Some History About Family Law

Until the early 1970s, spouses divided their property according to legal ownership when a marriage ended. However, several high profile cases highlighted the unfairness of the law. Possibly the most famous was the Supreme Court of Canada decision in *Murdoch v. Murdoch*. The Murdochs had, over the years, acquired substantial ranch holdings, all placed in the husband's name. The wife was active in all parts of running the ranch, as well as raising the children and looking after the home. Even so, the SCC held that the wife had no interest at all in the property the parties had acquired through their mutual efforts.

The unfairness of such a result was widely recognized and led, in the late 1970s, to Canadian jurisdictions enacting legislation giving courts power to divide matrimonial property, including pensions. The legislation, however, typically failed to say how pensions should be divided.

The initial methods adopted were 'judge made,' the member would pay the spouse compensation, or give another asset, in exchange for the pension interest.

Slightly more complicated was requiring the member to pay part of each pension payment to the former spouse once the pension started.

Neither of these methods of pension division involved the plan.

By the early 1980s, however, it was recognized that some plan involvement was necessary to achieve fair results and Canadian jurisdictions began enacting pension division legislation that provided, in way or another, for one spouse to be able to claim directly an interest in pension benefits owned by the other.

Methods Of Pension Division

Most Canadian pension division schemes are similar in the way they treat an 'un-matured' Defined Contribution pension plan and all matured pensions.

The spouse receives a share of an 'un-matured' DC plan immediately, by a transfer to a prescribed pension vehicle, such as an RRSP, based on the current value of the pension.

For a matured pension, most jurisdictions provide that the spouse receives a share of the income stream. The administrator makes separate withholdings and cuts two cheques, one for the member and one for the spouse. Quebec, in contrast, provides that the spouse's share must be satisfied by a lump sum transfer of the commuted value.

Where Canadian pension division legislation departs most markedly, however, is in the treatment of 'un-matured' Defined Benefit pension plans. Here the two main methods of pension division are the Immediate Settlement Method (ISM) and the Deferred Settlement Method (DSM). These are quite different in approach and philosophy.

Both methods usually determine the spouse's share by a formula – typically 50 per cent of A/B (where 'A' is pensionable service that accrued during the relationship and 'B' is all pensionable service that accrues up to the date the pension is divided).

Just as with un-matured DC plans, the ISM provides that the commuted value of the spouse's share in a DB plan is transferred from the plan immediately (to, for example, an RRSP). The pension is valued as of separation, assuming that the member terminated employment on that date and will retire at the normal retirement age (usually 65). If the benefits are vested, the transferred funds are locked-in.

In contrast, the DSM provides that the spouse must wait to receive the share until the member elects to have the pension commence. At that date, the spouse's share is based on the retirement value of the pension. Typically the spouse receives the share as a separate lifetime pension.

The ISM is substantially easier to administer than the DSM, but also places the lowest possible value on the spouse's share. The DSM places a more generous value on the spouse's share because it is based on the retirement value of the pension and takes into account the actual date of pension commencement. The DSM is also more effective than the ISM in ensuring that the spouse has income for old age. The ISM is more common in Canada. It has been adopted in Alberta, Saskatchewan, Manitoba, Quebec, New Brunswick, and for federal public sector pensions. The DSM is used in B.C., Nova Scotia, and Newfoundland and is also the method used for dividing CPP benefits. Ontario and PEI typically do not involve the plan in pension division, and compensate the spouse for a share of the pension through an equalization payment.

B.C.'s Legislation

In September 2005, the Ministry of Attorney General for B.C. asked the British Columbia Law Institute (BCLI) to review its pension division legislation (found in Part 6 of the Family Relations Act). The BCLI is a private, non-profit agency that functions as B.C.'s centre for law reform and policy development. A BCLI committee, consisting of experts in pensions, pension law, and family law, and representing the various stakeholders (plan administrators, advisors and regulators, and the family law bar), published its report in May 2006. It is available online at www.bcli.org.

The first question considered was whether the DSM should be continued or abandoned in favour of the ISM. It was concluded that:

- although there was an administrative burden posed by the DSM, fairness of result required continuation of the model
- the administrative burden had eased as experience had grown
- additional steps could be taken, through revising the legislation, to further improve matters.

In this respect, the BCLI reached the same conclusion as the Canadian Institute of Actuaries' Task Force.

Perhaps the most important issue addressed by the BCLI was the extent to which pension division poses unwarranted risk to plan administrators. One area in which the extent of liability cannot be comfortably predicted is where pension division arrangements have not been finalized, but the plan administrator has reason to believe that a member's marriage is ending and the spouse may be acquiring an interest in the pension. Can a plan administrator incur liability from constructive notice of the spouse's rights?

The BCLI recommended that no liability should arise until the plan administrator is provided with an agreement or court order, and prescribed forms, adequately addressing pension division.

Deferred Division

Because the essence of the DSM model is deferred division, there will be circumstances where a party may die and the pension is replaced by a death benefit, before division is completed. As with other Canadian jurisdictions, B.C. pension standards legislation requires a minimum pre-retirement death benefit (at least 60 per cent of the commuted value of the pension). Some plans provide a more generous death benefit. The minimum standard has only been in effect in B.C. since 1993, so it is possible for some plans to provide for no death benefit for accruals before 1993.

Although the parties should, they seldom take into account the generosity of the death benefits that will be paid in determining the spouse's share. In the absence of express direction, B.C. provides that the spouse is entitled to all of the death benefit that accrued during the relationship, determined on a pro rata basis. However, this may be far too generous, or completely inadequate, depending on how the death benefit is determined.

The BCLI recommended that the share the limited member receives should be the same, whether the pension or death benefit is divided.

In B.C., the spouse has two options for receiving a share of an 'un-matured' DB pension. The spouse may wait until pension commencement and take a separate lifetime pension, or the spouse may, at any time after the member becomes eligible to have the pension commence, elect to receive a lump sum transfer of the commuted value of the spouse's share.

The BCLI concluded that the lump sum option unnecessarily complicated matters. Many spouses lack investment experience and would prefer receiving a separate pension, leaving investment responsibilities to the plan. Also, some administrators reported that plan members were often upset that the lump sum transfer was available to the spouse, but not the member.

The BCLI recommended removing the lump sum transfer option and permitting the spouse to elect a separate pension at any date after the member becomes eligible to have the pension commence.

Currently, the spouse's share of an 'un-matured' DB pension is determined by assuming the pension commences at the valuation date. Some administrators of plans that provide subsidized early retirement benefits thought this approach substantially undercut the plan funding assumptions. The BCLI proposed dealing with this by providing that, if the spouse elects to take the pension before the member does, the share should be determined by assuming the pension commences when the member reaches the average age of retirement for plan members.

Need For Comment

In addition to these recommendations, numerous other proposals were made to fine-tune pension division, ranging from making beneficiary designations to dividing benefits in supplementary plans. Administrators and advisors of plans having B.C. members should make it a priority to review the BCLI report and provide comments (pro or con). Phase 1 of the consultation invites comments on proposals made by the BCLI for amending the rules governing pension division on marriage breakdown (available online at <http://www.ag.gov.bc.ca/>). The deadline for commenting on the Phase 1 consultation is May 31. ■

Thomas G. Anderson is a lawyer with Anderson Pension Law Consulting. He chaired the British Columbia Law Institute committee that reviewed the operation of Part 6 of the B.C. Family Relations Act.