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COMMUNIQUÉ

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ONTARIO ANNOUNCES KEY FEATURES OF THE ORPP

The Ontario government announced its decisions on many key design elements of the Ontario Retirement Pension Plan (ORPP) on 11 August 2015. This follows a consultation period during which only the high level features of the ORPP were available for discussion.

The Government's Policy and Plan

The government is creating the ORPP to address retirement income security as an alternative to expansion of the CPP, which the federal government has not been willing to do.

The ORPP is intended to incorporate the following features:

- A lifetime benefit so individuals will not risk outliving their savings;
- A benefit indexed to inflation to protect purchasing power over time;
- Mandatory employee and employer contributions reflecting a shared responsibility;
- Professionally managed investments that pool investment risk; and
- Locked-in retirement savings to ensure that they are used to provide retirement income.

In December 2014 the government issued a consultation paper asking for input on three key design considerations: whether to exclude employees who participate in other comparable pension plans or retirement savings vehicles; whether to mirror the CPP's minimum earnings threshold or adopt a different threshold; and how to help the self-employed achieve retirement income security. The province also held consultation meetings with various stakeholders and pension experts. The information announced on 11 August reflects decisions made by the government following this consultation. However, the announcements address the first of the three design considerations – the issues regarding the minimum earnings threshold and the inclusion of the self-employed are still being considered.

The government is committed to establishing the ORPP by 1 January 2017 and is expected to table legislation to implement this ORPP design after it returns to the house this September.

The balance of this Communiqué discusses the key design features of the ORPP combining information previously proposed and recently announced.

Coverage: Who Must Participate in the ORPP

The ORPP will be mandatory for Ontario employees in eligible employment who are age 18 – 70, and for their employers. Eligible employment will exclude federally regulated employees, employees receiving ORPP benefits and employees earning less than a minimum earnings threshold. Eligible employment will also exclude employees who participate in a comparable pension plan; however, the government is examining options for allowing employers with comparable pension plans to opt-in.

Comparable Plan

The principle behind the definition of comparable plan is that it is "expected to provide a predictable stream of replacement income and an adequate standard of living in retirement similar to the benefit that would be provided by the ORPP". The government determined that only registered pension plans would be considered as comparable plans due to the locking in provisions of these plans. Other retirement savings arrangements such as Group RRSPs, Deferred Profit Sharing Plans and Tax Free Savings Accounts will not be considered to be comparable plans.

Actuarial analysis was conducted to determine the following minimum thresholds that defined benefit and defined contribution registered pension plans must meet in order to be considered comparable.

Defined Benefit Plans:

- An earnings-based defined benefit registered pension plan must provide an annual accrual rate of at least 0.5%

- For a flat-benefit defined benefit registered pension plan, the 0.5% threshold will be determined as follows:

$$\frac{\text{Monthly Dollar Benefit Accrual} \times 12}{\text{Maximum Hourly Wage Rate} \times 2080 \text{ hours/year}} \geq 0.5\% \text{ accrual rate}$$

Defined Contribution Plans:

- A defined contribution registered pension plan must have total required employer and employee annual contributions of at least 8% of "base salary earnings", with at least 4% being contributed by the employer

- For a flat-dollar defined contribution registered pension plan, the 8% minimum contribution threshold will be determined as follows:

$$\frac{\text{Monthly Dollar Contribution} \times 12}{\text{Maximum Hourly Wage Rate} \times 2080 \text{ hours/year}} \geq 8\% \text{ contribution rate}$$

Hybrid Plans:

- For a hybrid plan that provides defined benefits plus defined contributions, the comparability threshold will be determined as follows:

$$\frac{\text{Annual DB Accrual Rate}}{0.5\%} + \frac{\text{Annual DC Contribution Rate}}{8\%} >= 1.0$$

- For a hybrid plan that provides the greater of a defined benefit or defined contribution formula, the minimum threshold for the defined benefit formula or the minimum threshold for the defined contribution formula must be met

Other Plan Designs

- For target benefit plans, multi-employer pension plans or pooled registered pension plans, the thresholds will be announced at a later date.

A process to verify which pension plans are comparable will begin in early 2016. Employers will be asked by the Ontario Retirement Pension Plan Administration Corporation (ORPP Administration Corporation) to provide relevant information.

Enrolment

ORPP participation will be required from date of hire. The enrolment requirement is based on an employee's participation (or non-participation) in a comparable plan. For example, ORPP participation would be required during a waiting period before the employee joins a comparable plan.

The government is examining options for allowing employers with comparable plans to opt into the ORPP. Additional details will be provided at a later date.

The government states that by 2020 every employee in Ontario (among eligible employees) will be part of either the ORPP or a comparable pension plan. Ontario also intends to provide the ORPP to the self-employed but this will not be possible without changes to the federal income tax laws applicable to registered pension plans.

Contributions and Phase-in

The fully phased-in contribution rate will be 3.8% of covered earnings shared equally by the employer and employee by payroll deduction.

The original proposal for defining covered earnings was:

- minimum: the same as the CPP YBE - $3,500.
- maximum: $90,000 in 2017, indexed to the YMPE under the CPP thereafter.

No new information has been provided about the minimum earnings threshold.

The announcement indicates that contributions will be introduced in four waves based on employer size and the existence of a registered pension plan as of 11 August 2015, with the first wave starting in 2017. The first three waves are for companies that do not currently offer a registered pension plan with the largest employers first. The fourth wave is for any employer that currently offers a registered pension plan for some or all employees. The later introduction date for companies with a pension plan provides additional time for these companies to amend their plans to become comparable prior to 2020. Both employers and employees will contribute at the following rates.

	Type of employer	2017	2018	2019	2020	2021
Wave 1	**Large** **500 or more employees**	0.8%	1.6%	1.9%	1.9%	1.9%
Wave 2	**Medium** **50-499 employees**	0%	0.8%	1.6%	1.9%	1.9%
Wave 3	**Small** **50 or fewer employees**	0%	0%	0.8%	1.6%	1.9%
Wave 4	**With non-comparable RPP**	0%	0%	0%	1.9%	1.9%

As the ORPP will be a registered pension plan, employee and employer contributions will be tax-deductible in the same manner as any other registered pension plan. The accrual of benefits under the ORPP will also result in Pension Adjustments being reported for each eligible employee.

Benefits

The objective is that the ORPP will provide a benefit that replaces up to 15% of covered earnings. The benefits will depend on the number of contributory years, the amount contributed and an individual's earnings during these years. Benefits will be locked-in, with portability features that are yet to be announced. Pensions will be payable for life and indexed to inflation. The normal retirement age is 65 with flexibility to start payments as early as age 60 or as late as age 70 with an actuarial adjustment. An important feature that is expected to be confirmed later is that the amount of benefits and the indexing of those benefits can be adjusted based on the financial position of the plan to ensure the long-term sustainability of the ORPP.

A buy back feature is proposed (but not yet worked out) to permit workers to purchase past service benefits for periods when they were unable to contribute.

The first benefit payments will begin in 2022.

Administration

The announcement does not contain details regarding the administration and investment management of the ORPP. However, the government intends to appoint an initial Board of Directors for the ORPP Administration Corporation in the coming weeks, which will be responsible for making these decisions.

Comment

This substantial new information enables employers to further assess their position. These assessments will inevitably raise further questions, but many more employers will now be able to determine whether they have comparable plans. Employers with workforces in Ontario and in other jurisdictions will also want to consider the implications of different treatment arising from the participation of Ontario employees in the ORPP.

Employers who have chosen to structure their retirement programs using Group Registered Retirement Savings Plans and Deferred Profit Sharing Plans face significant pressure in the short term, as they are expected to be compliant with the ORPP requirement beginning as early as January 2017 (for larger employers) and no later than January 2019 (for smaller employers).For employers with savings plans, significant effort will be needed to review the design and administration of their retirement programs, and determine what modifications are needed or desirable to facilitate participation in the ORPP by all eligible employees by the specified dates. For those who have savings plans covering employees in multiple provinces, and those with multiple retirement arrangements covering different employee groups, the issues will complex. Employee perceptions of any plan design changes will also need to be taken into consideration in communicating any changes. The impact on overall employer cost of switching to mandated contributions could be significant, as many defined contribution plans currently allow employees to determine the level at which they contribute, and structure employer contributions as a match based on employee's contributions.

Requiring a higher contribution under a defined contribution plan than is required under the ORPP, to be comparable, suggests that the government believes that defined benefit/target benefit plan designs, such as the ORPP, are a more efficient vehicle for delivering retirement income and can be expected to deliver more than a defined contribution plan for a given level of contributions. Employers with a defined contribution plan may find that some employees prefer the lifetime benefit provided under the ORPP while other employees prefer the flexibility to manage their own retirement savings under the current defined contribution plan.

Employers who begin to consider these issues from a business perspective should also be mindful of the impact of any changes on the financial well-being of their employees. Employers could take this time to review their retirement and savings programs from an overall employee financial wellness perspective, to inform their business decisions and to develop the communication of any program changes.

The originally proposed $3,500 minimum threshold for covered earnings, based on the CPP threshold, would likely have a negative impact on low income Canadians who can least afford increased payroll deductions – even if they relate to increased retirement savings. It will be critical for the government to consider the treatment of low income individuals, including the potential claw-back of income tested retirement benefits, before the minimum earnings threshold is finalized.

The future of the ORPP may also be dependent on the outcome of the federal election in October. The timing is very tight – but should the new federal government be open to CPP expansion in the near enough future, the ORPP might not materialize. Many would agree that a national solution is the preferable way to enhance Canada's retirement system.

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