

HEALTH WEALTH CAREER

SUPPLEMENTAL EXECUTIVE RETIREMENT PLANS IN CANADA

KEY FINDINGS FROM THE MERCER
SERP DATABASE (2014 UPDATE)

APRIL 2015



MAKE TOMORROW, TODAY





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1 INTRODUCTION

Many employers provide pension benefits through employer-sponsored registered pension plans. In Canada, the Income Tax Act places caps, or limits, on the level of pension that can be paid or the amount of contributions that can be made.

A supplemental executive retirement plan or supplemental employee retirement plan (SERP) is a pension plan that provides benefits in excess of the registered pension plan limits under the Income Tax Act.

Mercer maintains a database of the SERP practices of our Canadian clients in order to analyze current market practices and trends with respect to supplemental pensions. As of its most recent update, the Mercer SERP Database includes information from 415 organizations in a variety of industries and sectors (private, public, and not-for-profit). In order to maintain confidentiality, we do not disclose the identities of the organizations.

The database provides insight into the prevalence of SERP arrangements and current practice in both the design and financing of supplemental pensions. The database contains information on 360 SERPs provided by 240 organizations.

Breakdown of SERPs	Number in database
Defined benefit (DB)	270
Defined contribution (DC)	80
Hybrid or other	10
Total	360

We are pleased to present key findings from the database.

Relative value benchmarking of plans against plans in the database, as well as further plan design details, are available through your Mercer consultant, with breakdowns by:

- Eligibility criteria.
- Size of company (based on number of employees).
- Type of company (private sector with industry breakdowns, public sector).
- Type of SERP or registered pension plan (DB, DC, hybrid).

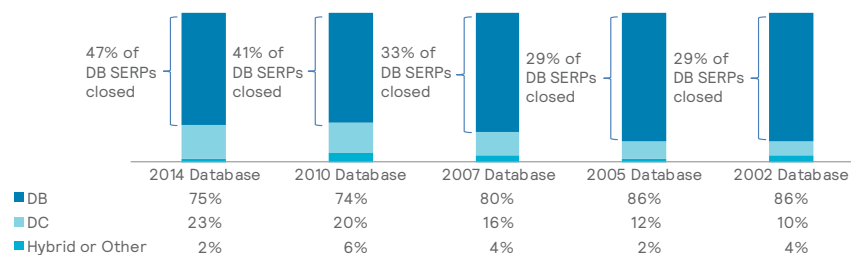
2 HIGHLIGHTS OF THE MERCER SERP DATABASE

Highlights from the SERP database include:

- Fifty-eight percent (58%) of organizations in the database sponsor at least one SERP. (Note: Companies in the database sponsor registered pension plans, so the prevalence of SERPs for companies in the database may overstate the prevalence of SERPs in the overall market.)
- As we have seen with registered plans, there is a trend toward closing DB SERPs to new members and opening DC SERPs.

Type of SERPs

Increase in DC SERPs; More DB SERPs Closing



- Larger organizations are more likely to sponsor a SERP.
- Half of SERPs now cover all employees affected by registered plan limits.
- For DB SERPs, an accrual rate of 2% of earnings per year of service is the norm, whereas there is a wide range of employer contribution rates under DC SERPs.
- The prevalence of bonus inclusion continues to be mixed, with about half of SERPs recognizing all or some bonus in pensionable earnings.
- The majority of SERPs vest immediately or at the same time as the registered plan.
- The proportion of companies prefunding or providing benefit security has been constant for many years now at about 50%.

3 KEY FINDINGS FROM THE MERCER SERP DATABASE

PREVALENCE OF SERPS

In the Mercer SERP Database, 240 organizations (58%) provide at least one supplemental pension arrangement. It is important to note, however, that since companies included in the database are sponsors of registered pension plans, it is likely that the prevalence of SERPs for companies in the database overstates the prevalence of SERPs in the overall market.

Company size continues to play a significant role in the prevalence of SERPs. Employers with at least 5,000 employees are twice as likely to provide a SERP as employers with less than 500 employees. The lower prevalence at organizations with less than 500 employees likely corresponds to the fact that these organizations have a smaller number of employees affected by the maximum pension limit and, as a result, may compensate for the impact of the limits through other elements of compensation.

Prevalence of SERPs by number of employees	2014 database
Less than 500	42%
500 to 5,000	71%
5,000 or more	84%
All	58%

ELIGIBILITY

Half of SERPs now cover all employees. The trend toward covering all employees developed over time. In some cases, this involved lowering the eligibility criteria for an existing SERP, and in other cases, a new SERP was established to mirror the registered pension plan.

Lowest level of SERP eligibility	All companies (240 companies)	Private sector (170 companies)	Public sector and not-for-profit (70 companies)
All employees	49%	48%	51%
Designated employees	45%	48%	39%
President/CEO only	6%	4%	10%
Total	100%	100%	100%

MIRROR VERSUS NON-MIRROR PLANS

The vast majority of SERPs that cover all employees affected by registered plan limits mirror all provisions of the underlying registered pension plan. For SERPs that cover only designated employees or only the president/CEO, the majority contain some provisions that differ from the underlying registered pension plan. Where SERP provisions differ, they are predominantly more generous (for example, inclusion of bonus in pensionable earnings, higher benefit formula or contribution rate).

SERP eligibility	Proportion of DB SERPs that are mirror plans	Proportion of DC SERPs that are mirror plans
All employees	80%	85%
Designated employees only	37%	49%
President/CEO only	10%	33%
All	51%	66%

BENEFIT LEVELS

DB Pension Accrual Rate

The maximum registered DB plan pension accrual rate permitted under the Income Tax Act is 2% of earnings per year of service.

Over half of DB SERPs covering all employees provide a 2% accrual rate, with the remainder providing less than a 2% accrual rate. By contrast, over 80% of DB SERPs covering designated employees or president/CEO provide a 2% or greater accrual rate.

DC Contribution Rate

The maximum registered DC contribution rate permitted under the Income Tax Act is 18% of earnings, inclusive of employee contributions. A typical registered DC plan has employer contributions of 5–6% of earnings.

The majority of DC SERPs provide the same employer contribution rate as they do under the registered plan. However, some DC SERPs provide an employer contribution on earnings not covered under the registered plan equal to the combined employer/employee registered plan contribution rates. Other DC SERPs, particularly for designated employees and presidents/CEOs, provide more generous employer contribution rates in the 10–20% of earnings range.

BONUS INCLUSION

Market practice on whether or not to include bonuses in pensionable earnings continues to be mixed, with approximately 55% of SERPs including bonus (typically full actual bonus). This mixed market practice is seen at small, medium, and large employers.

However, bonus inclusion is somewhat more prevalent in the private sector and less prevalent in the public and not-for-profit sectors. When the underlying registered plan recognizes bonus in pensionable earnings, the SERP almost always includes bonus as well. If, on the other hand, the underlying registered plan does not recognize bonus in pensionable earnings:

- For SERPs covering all employees, bonus inclusion is rare.
- For SERPs covering designated executives only, bonus inclusion is common.

The reasons to include or exclude bonus in the definition of pensionable earnings, and the extent to which the bonus is included, vary by company. These reasons tend to relate to the design of the bonus program and how bonus integrates with overall compensation.

It is important for compensation committees of the board to understand the financial impact of including bonus in pensionable earnings. This practice may dramatically increase the SERP liability.

VESTING

The majority of SERPs vest pension benefits at the same time as the underlying registered pension plan, particularly when the SERP formula matches the registered plan formula. However, longer vesting periods are more common for SERPs that provide enhanced benefits.

Percentage of DB SERPs that vest immediately or at the same time as the RPP	SERP formula matches RPP formula	SERP formula more generous than RPP formula
All employees	97%	100%
Designated employees	80%	49%
President/CEO only	33%	60%
Combined (all DB SERPs)	89%	54%

Percentage of DC SERPs that vest immediately or at the same time as the RPP	SERP formula matches RPP formula	SERP formula more generous than RPP formula
Combined (all DC SERPs)	89%	67%

FUNDING/BENEFIT SECURITY

In general, the proportion of SERPs that are prefunded or provide benefit security has been constant for many years. Benefit security is typically provided through funding of a retirement compensation arrangement (RCA) trust or purchase of a letter of credit to be held in an RCA in which the face amount of the letter of credit equals the SERP liability. Another option for DC SERPs is to payout the employer contribution annually, either directly to the member or to an after-tax account in the executive's name.

Prevalence of funding	DB SERPs	DC SERPs
Unfunded	55%	53%
RCA	32%	12%
Letter of credit	12%	8%
Paid to member or account	n/a	27%
Other	1%	0%
Total:	100%	100%

4 FOR MORE INFORMATION

For more information on supplemental executive retirement plans, please contact your retirement consultant or one of the following SERP specialists:

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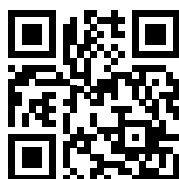
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