Alberta
Finance

Policy Bulletin #16
Plans for Connected Individuals

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This bulletin is designed to assist plan administrators, their consultants and legal counsel in understanding the provisions of the *Employment Pension Plans Act* (the Act) governing pension Plans for Connected Individuals. This document replaces the previous Bulletin "Plans for Specified Individuals" (PSIs) released December 2001. The Act and Regulation have been amended effective August 10, 2006, resulting in major changes to the regulation of these plans by the Superintendent of Pensions. Key sections of the Act and Regulation are Act sections 1(1)(hh.1), 14, 70 and 73 and Regulation Schedule 0.2, section 2.

This Bulletin has no legal authority. The Act and the *Employment Pension Plans Regulation* (the Regulation) should be consulted to determine specific requirements.

A new category of pension plan, the Plan for Connected Individuals, (PCIs) has been created under the Act. All filing requirements under the Act will no longer apply to this type of plan. This includes the requirement to:

- register the plan under the Act;
- file plan text amendments and funding agreements;
- file actuarial valuation reports and annual certifications;
- submit termination documentation (see page 4 for termination procedures); and
- comply with any other filing requirement under the Act.

Notwithstanding the discontinuation of these requirements, **all of the other standards set by the Act for funding, benefits, and disclosure to members and other beneficiaries still apply to these plans. Filing requirements with respect to the federal *Income Tax Act* (ITA) or Regulations ("the tax rules") have not changed. Therefore, administrators of these plans should be sure to familiarize themselves with Canada Revenue Agency requirements.**

What is a PCI?

A Plan for Connected Individuals is a pension plan whose active membership consists entirely of "connected persons" for the purposes of subsections 8500(3) of the *Income Tax Regulations* (Canada) CRC Vol X c945.

Section 8500(3) of the Income Tax Regulations defines a connected person as one who:

(a) owns, directly or indirectly, 10% or more of the issued shares of any class of shares of the employer or any other corporation that is related to the employer;

(b) does not deal at arm's length with the employer; or

(c) is a specified shareholder of the employer by reason of the ITA s. 248(1), the definition of "specified shareholder".

A person related closely to an owner by blood, marriage or adoption is considered to not "deal at arm's length" with the employer and is therefore also a "connected person". Because the members of PCIs are in a position to protect their own interests, there is a reduced need for regulatory scrutiny.

What is NOT a PCI?

Pension plans whose active membership consists of at least one non-connected person **do not qualify as a PCI**. For greater certainty, plans that are entirely comprised of members who earn more than 2.5 times the Canada Pension Plan's Year's Maximum Pensionable Earnings ($105,250 in 2006) **do not qualify as a PCI**.

Prior to the changes to legislation, plans that were comprised entirely of high earners would have been considered a plan for specified individuals. However, under the amended Act and Regulations, these types of plans do not meet the PCI qualifications and will be subject to all of the usual filing requirements and fees that are normally associated with pension plans. This includes the filing of Annual Information Returns (AIRs) and triennial valuation reports and cost certificates.

Legislative Requirements

Funding

The Act retains the definition of PSI, which includes both PCIs as well as plans where there are members who are not "connected" but who earn more than 2.5 times the YMPE. The reason for this inclusion is that all plans that qualify as PSIs continue to be subject to the minimum funding standards set out in the Act. **However, these plans are <u>also</u> subject to the maximum funding limits under the tax rules on both a going-concern and termination basis**, and therefore certain provisions of the Act permit exceptions to the funding rules for PSI's.

In addition to the funding of the normal costs of benefits, going-concern unfunded liabilities identified in regular valuations must be amortized over not more than 15 years; solvency deficiencies must be amortized over not more than 5 years, up to the maximum amounts permitted under the tax rules. To coordinate with the requirements of the *Income Tax Act*, actuarial valuation reports for PCIs may be completed once every 4 years, rather than every 3 years as currently required by the Act.

Qualifying Transfers

As was the case with PSIs, it has been necessary to co-ordinate administrative interpretations with CRA in cases where PCIs have money transferred in to purchase benefits not accrued due to active participation in the plan. Where CRA permits these amounts to be deposited to the pension fund, they are referred to as "qualifying transfers" (QTs).

Plan Suspension or Termination – Special Rules

Unlike the Act's requirements for other pension plans, suspension of the sole member or all the members, or the commencement of a pension by the sole member or all the members of a PCI do not automatically trigger plan termination. This allows the plan to remain in operation and pay out a pension to its members even when there is no active participation, or to delay purchase of a life annuity if prevailing interest rates are unfavourable. The plan, of course, cannot remain in operation unless there is an entity still in existence that qualifies as an administrator of the plan (see the definition of "administrator" in the Act), and that will remain financially responsible – normally the corporation employing the plan member(s). It is not, for example, an option where a professional corporation sponsoring a PCI for the professional ceases to exist once the professional retires.

In the case of a plan for an executive where the employer intends to continue the plan when the executive retires, the plan member must be informed that he has the option to have a life annuity purchased instead of taking a pension from the plan.

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