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Pensions as Net Family Property in Ontario: Issues and Considerations for Mediators

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This is a mediator-focused supplement to a paper entitled *Navigating the Pension Minefield Five Years Post Bill 133*, presented at the Simcoe County Family Law Lawyers' Association Conference in June of 2017, which can be found on the Publications/Papers tab at www.mckeating-actuarial.com.

Family Law Value of the Pension

For NFP purposes, pensions should be considered in four broad categories:

1. Ontario-registered plans:
- Search at http://planinfoaccess.fsco.gov.on.ca/
- For NFP purposes, this category would include plans registered in other provinces

2. Federally-registered plans:
- Employer is in the transportation, communication, or banking sector
- Employer is a crown corporation or other government spin-off (Canada Post, etc.)

3. Federal government employee plans:
- Federal civil servants, Armed Forces, RCMP, federal judges, Members of Parliament

4. Other plans:
- Non-registered supplemental top-up plans (for high earners)
- Foreign (US, UK, etc.)

Identifying the plan's category is an important early step. The category of plan determines who should provide the Family Law Value of the pension and what division options are available to the parties. It also assists the mediator in assessing the reliability of the Family Law Value that a party is proposing to use for NFP purposes.

The mediator should be on the lookout for:

- Administrator errors (more common than would be optimal)
- Unusual interpretations of the Ontario valuation rules by the valuator (administrator or actuary) that have a significant impact on the resulting Family Law Value
- Inadvertent non-disclosure of pension assets
- Use of pension values that are not Family Law Values, and that differ significantly from the prescribed FLV

The paper includes some high-level tips on how to spot problem valuations.

Net After-tax Value of the Pension

The Family Law Value is a before-tax amount. After the Family Law Value of the pension has been agreed-to by the parties, an income tax adjustment should be applied in order to convert the FLV of the pension to an "after-tax" value for insertion into the NFP statement.

The income tax adjustments that have been commonly used and accepted by the courts for many years are based on the party's average expected income tax rate in retirement. It is appropriate to use the same income tax adjustment for all of a party's registered retirement savings vehicles.

The most common of these "registered" or before-tax assets are as follows:

- Pension plans
- Registered Retirement Savings Plans (RRSPs)
- Locked-in Retirement Accounts (LIRAs)
- Deferred Profit Sharing Plans (DPSPs)

Tax-free Savings Accounts (TFSAs) are not before-tax assets, nor are most (but not all) employee savings plans. Income tax adjustments would not be applied.

If the parties' expected income in retirement differs, then the appropriate income tax adjustment to use for each party will also differ.

The mediator should be on the lookout for:

- Arbitrary income tax adjustments that may be too high (and unfair to the other side)
- Income tax adjustments based on marginal, rather than average, tax rates

Arbitrary income tax adjustments that are too low would be relatively unusual.

Division Options

There is no requirement under the Family Law Act to divide a pension for net family property equalization. In fact, the default is for no division to occur.

There are three major approaches to pension division:

1. LIRA transfers
2. Lump-sum transfer within the plan
3. Division at-source

In my opinion, a **LIRA transfer** should be viewed as the equalization solution of last resort in most instances. One exception to the caveat against LIRA transfers is when the plan member is seriously and terminally ill. If this is the case, a LIRA transfer may actually be the optimal equalization strategy. LIRA transfers are discussed more fully in the paper.

If available, a **lump-sum transfer within the plan** or an **at-source division** of the member's monthly pension can be helpful to achieving an equalization of NFP that works for both parties.

FSCO Form 4 Primer

Section 67.2 of the Ontario Pension Benefits Act requires the administrator of an **Ontario-registered pension plan** to determine the Family Law Value of a pension, if asked by either the plan member or the member's spouse.

If the administrator of an Ontario-registered plan is asked to determine the FLV of a pension, legislation requires that they use the FSCO-designed Family Law Forms (FSCO stands for Financial Services Commission of Ontario – the regulator of Ontario pension plans).

Unless the plan is Ontario-registered, there is no legal requirement to use these forms.

The general purpose of the forms is as follows:

- Forms 1, 2, 3: request a family law valuation from the administrator
- Form 4: provide a family law valuation to the parties
- Forms 5, 6, 7: tell the administrator whether or not there will be a pension division
- Form 8: used if a spouse wishes to give up their vested entitlement to an otherwise irrevocable spousal survivor pension (an unwise financial decision, in my opinion). In my opinion, this form should never be used.

The forms must be used in ascending numerical order. For example, the administrator of an Ontario-registered plan is not permitted to provide a Statement of Family Law Value (Form 4) unless they have received an application for the family law valuation (Form 1).

There are five versions of Form 4:

1. 4A: defined contribution plans (similar to RRSPs, values at marriage and separation can be determined without the Form 4A but the pension cannot be divided unless the administrator prepares a Form 4A)
2. 4B: defined benefit plans (members who are active participants in the plan, still accruing service)
3. 4C: "hybrid" plans which are a combination of defined contribution and defined benefit (active members)
4. 4D: defined benefit or hybrid plans (members who have terminated active participation but have left their pension entitlement within the plan, often called "deferred vested" members)
5. 4E: defined benefit plans (retired members whose pensions are in pay)

Page 2 of the **Form 4B** shows the Family Law Value of the member's pension, and the maximum transferable amount. If a LIRA transfer is a permitted option, note that the amount on page 2 is a maximum. It is not an "all or nothing" amount.

Page 2 of the **Form 4E** shows the Family Law Value of the member's pension and the Family Law Value of the spouse's survivor pension (if applicable). The maximum amount for a monthly at-source division is presented on pages 2 and 3. Again, this is a maximum. It is not an "all or nothing" amount. If the parties agree that the spouse should receive the maximum at-source division, this is equivalent to the member paying a before-tax equalization payment of 50% of the Family Law Value of the member's pension. It should be noted that the maximum does not take the FLV of the of the spousal survivor pension into account. For example:

Member's pension	FLV = $400,000
Spouse's survivor pension	FLV = $100,000

If the maximum at-source division is implemented, this is akin to the member making a before-tax equalization payment of $200,000. The result would be, for NFP purposes, that the spouse ends up with pension property valued at $300,000 ($200,000 from the member's pension and $100,000 from their spousal survivor pension) and the member ends up with $200,000.

It may be helpful to think of FSCO **Forms 5 and 6** as covering memos to the copy of the separation agreement that is sent to the plan administrator. These forms are not intended to be stand-alone documents and they do not typically form part of the formal separation agreement. Rather than inserting amounts or percentages into Form 5 or 6 – which may lead to unintended consequences, it may be advisable to refer the reader to the attached separation agreement. This will ensure that the plan administrator carefully reviews the actual separation agreement wording and implements the intent of the parties as documented in that agreement.

Interest on Equalization Payment from Pension Plan

There is much confusing over the question of whether or not interest should be paid if some or all of the equalization obligation is being paid by means of a LIRA transfer or a lump-sum transfer within a pension plan.

In addressing this issue of interest, the parties may wish to consider whether or not interest would be paid if the equalization payment was being made in cash. The 2014 *Heringer* decision confirms that there is no obligation to pay interest on an equalization obligation simply because the obligation is being satisfied by means of a LIRA transfer rather than by cash. Paying interest is neither the default nor is it required. The rules regarding equalization payments are the same, whether the payment is made in cash or from a pension plan or RRSP.

Separation Agreements

The agreement should set out the intent of the parties and provide clear instructions regarding any actions that the plan administrator is to take.

If the pension-related paragraphs of a separation agreement or Order are incomplete or ambiguous, the administrator may send the agreement or Order back because it cannot be implemented as written (bad) or they may decide to guess the intent of the parties (worse).

The paper includes checklists, and tips on what to do and what not to do when drafting the pension-related sections of a separation agreement.

Final Words

Mediators may be reluctant to involve an actuary in a family law matter due to cost considerations or concerns over how the party who finds himself or herself “disadvantaged” by the actuary’s input might react.

However, pensions are complicated. The Ontario valuation rules are complicated. After almost six years, there are few, if any, legal decisions that address the more contentious and ambiguous aspects of the legislation. If, unbeknownst to the mediator and the parties, an agreement is grossly unfair to one party due to a pension-related error or oversight, significant problems may ensue if and when the error or oversight is uncovered at a future date.

Mediators, like family law lawyers, should not hesitate to seek the assistance of their favourite actuary if and when required.

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