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# Final Federal Pension Investment Rules Released

## An Overview of Key Changes

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Earlier today, the federal Department of Finance published the final text of changes to the *Pension Benefits Standards Regulations,1985* (PBSR), which include significant changes to the federal investment rules (FIR).[1] The FIR are set out in Schedule III to the PBSR and affect most Canadian pension funds.

These new regulations implement Finance proposals that were originally announced in 2009 and 2010, and are designed to modernize the pension fund investment rules. A draft of the amendments to the PBSR was pre-published in September 2014 for a 30-day comment period. Finance received 19 written submissions from plan sponsors, pension fund managers, industry associations, members of the legal and actuarial professions and a retiree association, most of which focused on the proposed changes to the FIR.

Finance has delayed the coming-into-force date of the FIR changes described in this bulletin until July 1, 2016 to give plan administrators time to adjust their compliance systems and practices.

The key investment rule changes are as follows:

- ***Related Party Rules*:** The current rules prohibit a plan administrator from investing or entering into a transaction with a related party of the plan. One important exception to the current rules permits the administrator of a plan to enter into a transaction with a related party if the value of the transaction is nominal or the transaction is immaterial to the plan. Finance had proposed eliminating this exception. However, in a move that will be applauded by plan administrators, Finance has decided to leave the nominal or immaterial exception in place in light of stakeholder concerns that the elimination of this exception would result in significant administrative burden and might impact administrators' ability to invest in a prudent manner.

  One current exception to the related party rule permits the administrator to purchase securities of a related party if those securities were acquired on a public exchange. The new rules remove the public exchange exception and instead allow the administrator to invest in the securities of a related party if the securities are held in an investment fund or segregated fund in which investors other than the administrator and its affiliates may invest and which complies with certain quantitative limits.

  The new rules also clarify that the administrator may enter into a "transaction" with a related party for the administration of the plan (such as hiring a related party to act as a broker dealer) as long as the transaction is under market terms and conditions and does not involve the making of loans to or investments in the related party. Finance had previously proposed limiting this exception to only cover "engaging the services" of a related party.

  The new rules also introduce an exception to the related party rules applicable to investments that involve the purchase of a contract or agreement in respect of which the return is based on the performance of a widely recognized index of a broad class of securities traded at a marketplace (Marketplace Exception).

- ***10% Concentration Limit*:** The current rules prohibit a plan administrator from investing or lending more than 10 percent of the total book value of a plan's assets in any single entity or affiliated or associated entities. As anticipated, under the new rules, the calculation will be based on "market value" instead of "book value."

  In response to several stakeholder requests for clarity on the application of the 10% concentration limit, the rule has been amended to make clear that it is intended to apply to any transaction that would result in the plan exceeding the limit; i.e., it is not intended to be an ongoing "ever-green" test. This is a helpful clarification as it confirms the view held by many pension plan administrators. The changes coming into force afford some new relief by providing that the Marketplace Exception to the related party rules described above will also apply as an exception to the 10% concentration limit.

- ***Deeming Rule*:** Under the current rules, investments made by "a mutual or pooled fund or trust fund in which the moneys of the plan have been invested" are deemed to be investments indirectly made by the administrator of the plan. The language used in this phrase has been modernized to refer instead to investments made by "an investment fund, a segregated fund or a trust fund in which the moneys of the plan have been invested." The new rules define "investment fund" as follows:

  > "investment fund" means a fund — established by a corporation, limited partnership or trust — the purpose of which is to invest the moneys of two or more investors and the shares or units of which are allocated to each investor in proportion to the interest of the investor in the assets of the fund.

  This new definition broadens the scope of the deeming rule by clearly including investments held through funds regardless of whether they are in corporate, limited partnership or trust form.

The final text of the changes to the PBSR, including the changes to the pension investment rules described above, is available here.

If you have any questions with respect to the amendments to the FIR, please contact the authors.

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[1] Finance also published other amendments at the same time that are intended to improve the regulatory framework for defined contribution pension plans and disclosure to plan members and beneficiaries. Torys will be publishing a separate client bulletin on these changes at a later date.

*To discuss these issues, please contact the author(s).*