ALBERTA
LAW REFORM
INSTITUTE

DIVISION OF PENSION BENEFITS UPON MARRIAGE BREAKDOWN

Consultation Memorandum

September 1995

ALBERTA LAW REFORM INSTITUTE

The Alberta Law Reform Institute was established on January 1, 1968, by the Government of Alberta, the University of Alberta and the Law Society of Alberta for the purposes, among others, of conducting legal research and recommending reforms in the law. Funding of the Institute's operations is provided by the Government of Alberta, the University of Alberta, and the Alberta Law Foundation.

W.H. Hurlburt, Q.C. is a consultant to the Institute and a member of the Institute's Board. He has carriage of the project on Division of Pension Benefits.

PREFACE AND INVITATION TO COMMENT

This is a Consultation Memorandum. The Institute's purpose in issuing a Consultation Memorandum at this time is to allow interested persons the opportunity to consider these issues and to make their views known to the Institute. Any comments sent to the Institute will be considered when the Institute determines what final recommendation, if any, it will make.

The reader's attention is drawn to the questions which are set out in highlight boxes. It would be helpful if comments would refer to these questions by number where practicable, but commentators should feel free to address any issues as they see fit.

It is just as important for interested persons to advise the Institute that they approve the proposals as it is to advise the Institute that they object to them, or that they believe that they need to be revised in whole or in part. The Institute often substantially revises tentative conclusions as a result of comments it receives. The proposals do not have the final approval of the Institute's Board of Directors. They have not been adopted, even provisionally, by the Alberta government.

Comments on this memorandum should be in the Institute's hands by **January 15, 1996**. Comments in writing are preferred. Our address is:

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Consultation Memorandum

I. INTRODUCTION

A. Purpose of Memorandum

In 1986, ALRI issued its Report 48, *Matrimonial Property: Division of Pension Benefits upon Marriage Breakdown* ("Report 48"). We now propose to review the recommendations that we made in Report 48 in order to see whether and how they should be revised under present circumstances.

The purpose of this memorandum is to solicit comments and advice on the whole subject and, in particular, on the recommendations that we made in Report 48 and as to the recommendations that we might make now.

This memorandum is prepared by ALRI staff and the views expressed in it have not been considered or approved by the ALRI's Board. The results of our solicitation of comments and advice will be provided to the Board as the basis for its discussion of the issues raised.

B. Reasons for Review

It is settled policy and settled law that pension benefits which accrue to spouses during a marriage are part of the matrimonial property that is to be distributed between the spouses on marriage breakdown under the Matrimonial Property Act.[1]

Report 48 made recommendations for changes in the law to make the division process fairer, more efficient and less costly and to protect the interests of all concerned, including spouses, other beneficiaries, employers and plan administrators. We believe that, if they had been enacted, they would have achieved these purposes.

The Government has given active consideration on a number of occasions to the recommendations of Report 48. We are not aware of any dissatisfaction with the recommendations themselves, but they have never quite made it to the stage of legislation. One possible difficulty is that we recommended that they be

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[1] R.S.A. 1980, c. M-9.

implemented by amendments to the MPA, and opening that Act to amendment has the potential for raising unrelated controversial issues.

Much has happened since 1986, when we issued Report 48:

- Legislation enacted federally and in other provinces has provided working models of pension division which should be examined, though they fall generally within the pattern of Report 48.
- The Law Reform Commission of British Columbia has issued a report on the subject[2] and British Columbia legislation has substantially adopted the Commission's recommendations. While the methods of pension division available under the LRC's proposals are not on the whole very different from those recommended in Report 48, there is one significant policy difference, which affects some of them: under the LRC's proposals, the spouse who is not a pension plan member will share in post-division improvements in the pension benefit.
- The Ontario Law Reform Commission has also issued a report on the subject,[3] which would also allow the non-member spouse to share in the post-division benefits.
- Vested but unmatured pension benefits under Alberta pension legislation have, with some qualifications, become "portable", that is, a pension plan member who terminates their membership can have the present value of the pension benefit paid out from the pension plan to another registered pension vehicle in the name of the member. This provides machinery for the payment of a share of the present value to a non-member spouse's registered pension vehicle.

The immediate occasion for our review is the work of The Alberta Employment Pension Plans Administration Advisory Committee. This Committee, as its title indicates, is an advisory body to the Superintendent of Pensions for Alberta. It has identified as a major concern the problem of division of pensions on marriage breakdown. This concern arises because "unclear and contradictory

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[2] *Report on the Division of Pensions on Marriage Breakdown*, LRC 123, 1992 ("the BC Report").

[3] *Report on Pensions as Family Property: Valuation and Division*, 1995 ("the Ontario Report").

legislation combined with confusion about the issue in the legal community, has led to inappropriate costs and distress for all concerned".[4]

AEPPAAC has, in effect, urged ALRI to undertake the present review with a view to alleviating the costs and distress that the Committee has identified. Its suggestion is that, while the recommendations in Report 48 were a useful response to conditions that obtained in 1986, require review and some revision to make them appropriate to the conditions that obtain in 1995. The Committee's views are referred to in detail later in this Consultation Memorandum.

ALRI remains of the view that reform of the law relating to the sharing of pension benefits on marriage breakdown will serve the interests of all concerned—pension plan members, spouses of pension plan members, and pension plan administrators and sponsors. We have therefore undertaken to review our recommendations in order to see whether and how they should be revised in the light of changes in the legislative and pension environments since 1986.

C. Procedure

Our first step in the review is the preparation of this Consultation Memorandum. The Memorandum will set out the relevant issues. It will set out the relevant considerations. It will ask readers to give us their comments and advice.

We will then circulate this Consultation Memorandum for review and comment by those affected by the division of pensions on marriage breakdown. If there are groups of pension members or spouses of pension members, we would like to get their views. We can and will consult the bar, both because of its special position, and because lawyers can give useful information and comment about the needs of their clients. We will obtain the views of pension plan administrators and Government administrators.

Having consulted those affected, we will prepare revised recommendations and issue a revised report, though we will consult further before doing so if necessary.

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[4] Letter, Elaine Noel-Bentley, chair of the Committee, to Alberta Law Reform Institute dated Jan. 5, 1995.

D. Structure of This Consultative Memorandum

This Consultative Memorandum consists of a series of questions which we think are raised by post-Report 48 developments, including some important points raised by the LRC BC and OLRC reports, and including some suggestions that have been made to us. Under each question we will set out the considerations and arguments that we think are relevant to the question and state our present views. Then we will invite comment.

We intend the questions to provide a structure for consideration of the subject. A reader who thinks that we have not framed a question appropriately or that we have not asked the right questions should say so. Otherwise, we hope that readers will direct their comments to questions as framed.

Before setting out the questions, we state one premise. It is that a spouse's pension benefit accumulated during marriage is included in the property to be divided between spouses under the Matrimonial Property Act on marriage breakdown. This is a given. The project is about what is included in a pension benefit and how a pension benefit can most efficiently and fairly be divided between a plan member and a non-member spouse.

We have attached as an appendix the recommendations that we made in Report 48. A reader might find it useful to look through these recommendations with two purposes in mind. One is to get an overview of the subject as we perceive it. The second is to see whether any recommendations should be reviewed other than those covered by the questions we will pose.

E. Terminology

In Report 48 we used some terms that are not in general use. We think that the path of least confusion is for us to continue to use them. We will explain them here.

Valuation and accounting

When matrimonial property is to be divided under the Matrimonial Property Act, the usual approach is to prepare a statement showing the value of the matrimonial property held by each spouse. The one with the greater share must then pay money or transfer property to the other so that each has the appropriate share (presumptively 50%). We have called this process "valuation and accounting". The LRC BC report uses the term "compensation payment" and the OLRC report uses the term "equalization payment".

Valuation and division

Report 48 recommended that a new form of pension division be made available. Under it, the pension benefit would be valued, and the non-member spouse's share would be transferred by the pension plan to a registered pension vehicle in the name of the non-member spouse. Note that this involves a division of the pension asset itself, though by means of a dollar transfer, so that the pension benefit would not be shown on the statement of account between the spouses in a valuation and accounting of other divisible matrimonial property. We called this "valuation and division". The LRC BC appear to include it as one alternative form of an "account split", though their "account split" is deferred until the plan member can retire.

The OLRC have proposed a form of division at source by transfer which resembles "valuation and division". It is, however, different, as it envisages the use of money paid out of the pension plan as part of the equalization payment required by a valuation and accounting. That is, the pension benefit would appear as an asset in the plan member's column, and the money from the plan would then make up part or all of the equalization payment. We discuss such a proposal later in this Consultation Memorandum.

Provision of a separate pension

Report 48 recommended that another new form of pension division be made available, which we called "provision of a separate pension". Under it, the non-member spouse's share of the pension benefit as it stood at the time of division of the matrimonial property would, at a time when the plan member could retire, be translated into a pension from the pension plan in the name of the non-member spouse and based on elections made by the non-member spouse. Here, the pension benefit would be divided in specie.

The LRC BC has included a similar proposal as the other alternative form of "account split". Its proposal is different in that it gives the non-member spouse the benefit of post-division improvements in the pension benefit up to at least the first time at which the member could retire.

Division of proceeds

This term is self-explanatory. Under "division of proceeds", money paid out from the pension plan under its terms, whether pension or other money benefits, would be divided between the plan member and the non-member spouse according to

their respective shares in the pension benefit. A court order that provides for this is sometimes called an "if and when" order.

II. DISCUSSION OF ISSUES

A. Premise

> *A spouse's pension benefit accumulated during marriage is included in the property to be divided between spouses under the Matrimonial Property Act on marriage breakdown.*

It is settled policy that a pension benefit is divisible matrimonial property. It is also settled law. This project accepts it as a given.

B. What is to be Paid for or Shared?

> ***Question 1: Post-division changes in pension benefit.***
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> ***Where a plan-member spouse has a vested right to a deferred pension,***
>
> ***(a) should the prospect of post-division changes in the pension benefit be taken into account in valuing the non-member spouse's share of the pension benefit?***
>
> ***(b) should the non-member spouse share in post-division changes in a pension benefit which in fact occur?***

1. ALRI's view

Essentially, ALRI's Report 48 recommended that a pension benefit that includes a vested right to a deferred pension[5] be valued or shared as it stood at the time of the division of matrimonial property. The prospect of post-division changes in the benefit, whether as a result of increases in the member's salary or because of improvements made to the plan, should not, in ALRI's view, be included in the valuation of the benefit, nor should actual changes affect the amount received by the non-member spouse under a separate pension or division of proceeds.

Of course, if, at the time of division, a member has a right to a post-division improvement, that right would be part of the pension benefit.

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[5] The valuation of an unvested right is discussed separately below.

Suppose, for example, that a defined benefit plan provides at "normal" retirement date a pension of 2% of the average of the plan member's last 5 years' salary for each year of pensionable service. Suppose further

- that at the time of division of matrimonial property the plan member has 10 years' pensionable service and their average salary for the last 5 years was $30,000. At that time, the plan member would be entitled to a deferred pension of 0.02x10x30,000, or $6,000 for the marital years.
- that at the "normal" retirement date, the plan member has 20 years' pensionable service (including the 10 marital years and 10-post-marital years) and their average salary for the last 5 years was $40,000. At that time, the plan member would be entitled to a deferred pension of 0.02x20x$40,000, or $16,000, of which, on the face of it $8,000 was attributable to the marital years.

Post-division improvements to the plan might increase the deferred pension even more.

ALRI did not set out at length its reasons for recommending that post-division changes not be taken into account, saying merely that

> the greater unfairness would be in allowing a non-employee spouse to share in increases in the pension benefit which arise and are paid for after the time of division of the matrimonial property.[6]

Since the time of Report 48, the Law Reform Commission of British Columbia and the Ontario Law Reform Commission have issued careful and thorough reports on the subject of pension division on marriage breakdown. The two Commissions, like ourselves, have tried to devise fair and efficient ways of dividing pension benefits on marriage breakdown, and there is much common ground between us. There is, however, an important divergence of view between the two Commissions and ALRI. The LRC BC and the OLRC are of the view that a non-member spouse should share in increases in a pension benefit that accrue after the division of matrimonial property because of post-division improvements made to the pension plan or because of post-division increases in the plan member's earnings. We are of the view that the non-member spouse should not share in such increases. However, we think that the fact that the two commissions

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[6] Report 48, at 13. A minority of ALRI's Board would have allowed post-division sharing in a case in which the plan member opposes a valuation and accounting and the non-member spouse is locked into a deferred pension or share of proceeds.

have come to the opposite conclusion makes it necessary to canvass the subject again and review that conclusion.[7]

Because of this divergence of view on an important policy issue we will set out at some considerable length the views of the LRC BC, the OLRC and ourselves. The discussion initially relates to the valuation of a pension benefit for the purposes of what is referred to by the LRC BC as a "compensation payment", by the OLRC as an "equalization payment", and by ourselves as "valuation and accounting". It goes on to deal briefly with valuation for valuation and division and with sharing by division of proceeds.

2. Valuation and accounting: The views of LRC BC and OLRC about valuation

We will first set out the reasons of the British Columbia and Ontario Commissions for the view which they hold.

The British Columbia Report says at page 35:

> We addressed the pros and cons of [the policy of dividing increases in a pension account that occur after marriage breakdown between spouse and member] fully in the Working Paper. We remain convinced that the correct policy is to protect the value of the divided pension.

The accompanying footnote says:

> See particularly Appendix C to the Working Paper.

The passage in Appendix C to the British Columbia Working Paper that deals with sharing in post-valuation increases in value of a pension benefit is as follows (not including footnotes, which are references):

> Four arguments are usually raised in this context:
>
> 1. In terms of principle, the court is dividing wealth at the time of marriage breakdown. This suggests that changes in the value of a pension after that time are irrelevant.
> 2. Moreover, it is less speculative to calculate the value of the pension as if retirement occurred on the valuation date (the "termination method") rather than the predicted retirement date (the "retirement method.")
> 3. On the other hand, it may be observed that, insofar as a "final or best average earnings" defined benefit plan is concerned, each year during which entitlement is earned should produce an equal percentage of the final or best average earnings, even if they have to be estimated. The first years in which entitlement is earned are of equal importance to the later years. The spouse is undercompensated if entitlement is determined by reference to an earlier salary level (or without reference to expected indexing or other future adjustments to the pension).

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[7] The arguments are discussed at greater length in Pask & Hass, *Division of Pensions*, (Carswell, 1990) III-18 to III-22.

4. Changes to a pension aren't really changes in its value, but are often designed to off-set inflation.

Presumably it is arguments 3 and 4 that convinced the British Columbia Commission that post-division changes in value should be taken into account (though for valuation for a compensation payment—ALRI's "valuation and accounting"—it appears that prospective changes are to be considered only if they **increase** the value of the pension benefit).[8]

The Ontario Commission's reasons for taking post-division changes in pension benefits into account in valuing a pension benefit are given in the following passages:

> **Page 104**
> The use of the retirement method in calculating the present value of the pension plan provides a more accurate indicator of the value of the pension benefit accrued during marriage than does the termination method. The termination method artificially assumes that the pension asset will cease to accrue after the separation of the spouses, whereas the retirement method takes into consideration every year of plan membership.
>
> **Page 105**
> The retirement method produces a more accurate value of pension assets, thereby ensuring that both spouses enjoy a reasonable measure of income security in their future years. Moreover, calculations that account for future changes in the value of an asset are not necessarily inconsistent with the *Family Law Act* scheme if the value is assigned to the portion of the pension entitlement that accrued during marriage.
>
> **Page 176** (after referring back to the previous passages)
> In addition, using the value of the pension at retirement to satisfy the more general equalization payment provides a larger pool of resources to the member spouse to satisfy an equalization obligation. It also ensures that the value placed on the pension for *Family Law Act* equalization purposes will be satisfied through pension division at source.

3. Valuation and accounting: ALRI's reasons for not taking post-division changes into account

a. Assumption that pension asset will cease to accrue

As a preliminary point, it will be noted that the passage quoted above from page 104 of the Ontario Report gives as a reason for preferring the "retirement" method that "the termination method artificially assumes that the pension asset will cease to accrue after the separation of the spouses". ALRI does not make that assumption. ALRI's view is that post-division accruals are earned by the member during the post-marital years and do not represent an accumulation during the marital years. What the member would have if he or she were to terminate employment is, we think, the appropriate measure, but that is because what the

[8] BC Report, Draft Reg. 13(c), at 106.

member would have if they did not provide post-division employee services is a measure of what **was** accumulated during the marital years.

Indeed, it is the "retirement" method that requires additional assumptions. As the OLRC says:[9]

> The retirement method introduces an added element of speculation into the pension valuation process because it is based on a number of assumptions, such as the continuing employment of the member and expected salary increases.

While actuaries do make such assumptions in providing advice as to the funding of deferred benefit pension plans, there is room there for annual corrections as experience diverges from the assumptions, but there is no such room in an individual case.

Taking into account post-division ad hoc plan improvements requires further assumptions.

b. Income security

Another point made by the OLRC is that valuation at "retirement value" produces a more accurate value, "thereby ensuring that both spouses enjoy a reasonable measure of income security in their future years".[10] But it seems to us that the only necessary effect of using "retirement value" rather than "termination value" is to increase the equalization payment which the plan member must make or to decrease the equalization payment which the non-member must make, depending on which spouse has the greater share of the divisible matrimonial property.

If the further step of using the pension benefit to pay all or part of the equalization payment is taken, the non-member spouse will receive part of the pension income. Whether this will give the non-member or member spouse a reasonable measure of income security will depend on the amounts involved and the way in which they divide the benefit of the pension asset.

c. ALRI's analysis of valuation

i. GENERAL APPROACH

For valuation purposes, the LRC BC and the OLRC attribute post-division increases in a pension benefit to the marital years. ALRI attributes them to the post-division years. Essentially, that is the reason for the difference in conclusions.

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[9] Ontario Report, at 106.

[10] See the quotation from p. 105 above.

Our view is that

- at the time of division the member has only earned and acquired the benefit that the pension plan gives the member at the time of division;
- if post-division increments occur, it is because the member buys them by their post-division money contributions and employment services; and
- requiring the member to pay the non-member spouse for post-division improvements which the member must subsequently purchase from the pension plan by contributions and services is not equitable.

We will give our reasons for these views.

ii. WHAT A VESTED UNMATURED PENSION BENEFIT CONSISTS OF

The matrimonial property that should be divided between spouses at marriage breakdown is the property that has been accumulated during the marriage. That proposition applies to pension benefits as well as to other matrimonial property.

A vested unmatured pension benefit includes a right to a deferred pension payable on a specified retirement date, or, more usually, to one of a number of different pensions payable on one of a number of different retirement dates,[11] if the plan member survives. Under a defined benefit plan the amount of pension earned at any given time is determined by the defined benefit formula. If a plan gives members additional rights, such as a right to an indexed pension, those rights are part of the pension benefit and are included in the divisible property. In our view, that is the extent of what the plan member has at division time and the extent of what should be treated as divisible under a valuation and accounting.

If the plan member does nothing—that is, does not provide employment services and (if the plan is contributory) pays no contributions—there will in most defined benefit cases be no increase in the deferred pension after the time of division of matrimonial property. An increase in benefit that depends on the plan member providing future services and making future payments, unless the plan member already has a right to those increases, is not, in our view part of what the member has at the time of division. It is true that increases in pension due to increased post-division earnings and post-division plan improvements will apply to the whole of the member's pension benefit, but that is, in our view, due to post-

[11] Of course, the pension benefit is likely to include death and other benefits, but they do not enter into this discussion.

division events and is not inherent in the marital years as part of the pension benefit at the time of division.

iii. WHAT PAYS FOR POST-DIVISION INCREASES AND IMPROVEMENTS

At the time of marriage breakdown, if vesting has taken place, the plan member has bought and paid for a quantifiable deferred pension. Under a defined contribution plan, the pension is quantified by the credit to the pension account. Under a defined benefit plan, the pension is quantified by the defined benefit formula. If the plan is a contributory one, the member has paid part of the purchase price of the deferred pension by making the required employee contributions. The member has paid all or the remaining balance of the purchase price indirectly, through employer's contributions which the member has bought and paid for by employment services.[12]

Any post-division increase in the deferred pension must also be bought and paid for. At the the time of division, a post-division increase has not been paid for. If the plan is a contributory one, the member will pay part of the purchase price of the deferred pension by making the required post-division employee contributions. The member will pay the balance of the purchase price indirectly, through employer's contributions which the member has bought and paid for by post-division employment services.

This is pointed up in the case of post-division increases in a deferred pension which require increased contributions. First, we are told that there are some defined contribution plans under which contributions escalate with years of service. Second, in many defined benefit plans, the employer and employee contributions are fractions of earnings, so that the higher earnings that attract a higher deferred pension also require higher contributions. The higher employee contributions are paid by the employee, and the higher employer contributions are purchased by the employee through employee services. We do not think it fair that a non-member spouse who has not shared in the burden of a post-division increase in contributions should share in the benefit that flows in part from those contributions.

We think that, although less obviously, the same reasoning applies to all post-division contributions and not merely to the increase in post-division

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[12] The deferred pension depends on the survival of the plan member to a retirement date provided for in the plan, but that is not relevant to this discussion.

contributions. In order to get a post-division increase in the deferred pension, the employee must provide employee services and normally must make the post-division employee contributions and purchase the post-division employer contributions. If the member does not do this, the increase will not be earned.[13]

iv. Pension benefits as part of economic package

Pension plans call for contributions by the employer. These are part of the economic package which an employer makes available for all employees of specified classes.

An employer's cost of labour includes salaries. It also includes employee benefits such as employer's pension plan contributions. Employers are not likely to fail to notice this fact. It is safe to assume that they tend to think of salaries and benefits as part of one economic package. It may not follow that the payment of a dollar in employer pension contributions causes a reduction of exactly a dollar in salaries, but it seems to us to be unsafe to assume that employers will pay the same salary if they pay more money towards benefits. Salaries and benefits are interrelated. If the employer were not making pension plan contributions it is likely that the employer would pay higher salaries because the ability of employees to command compensation is likely to be much the same no matter how the compensation is divided between salaries and benefits. Employer contributions are not cost-free to employees. We think that requiring the member, through valuation and accounting, to pay the non-member spouse for benefits that the member must then buy from the pension plan, with no sharing of the burden by the non-member spouse, is not equitable.

Again, we consider first the case in which an employee's salary is increased with a resulting increment to a defined benefit pension benefit. The increase requires the employer's concurrence. It entails not only the increase in salary but the consequent increase in pension contributions. An employer may—and, if the amount is significant is likely to—take into account the incidental increase in pension benefit cost in determining the amount of salary increase that the employer is willing to provide.

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[13] We understand that it is customary to calculate the contributions to a final earnings plan so that the fund will be sufficient to provide pensions based on projected higher earnings to those members who reach retirement age, subject to the effect of provision for terminations and for death benefits. Since it is the defined benefit formula rather than the funding provisions which increases a member's entitlement, we do not think that this circumstance is relevant to the discussion.

Again we think that similar reasoning applies to all the employer's post-division contributions and not merely to those attributable to increased earnings. The employer's contributions are part of the plan member's current economic package. The employer makes them as part of the total current economic package for employees. The member earns them as part of the economic package. The member earns them through post-division employee services. The member bears the entire burden of ensuring that the employer's post-division contributions will be made. The non-member spouse bears none of it. We do not think it right that the non-member spouse should share in future increments purchased by the member spouse by providing post-division employee services. The employer's contributions, earned by the employee's post-marital services, are the second part of the purchase price of the additional pension benefits.

v. The effect of the marital years

Under many defined benefit formulas, the number of years of pensionable service is one multiplier and an earnings number is another. An increase in the earnings number will increase the whole pension benefit. But that is not to say that the marital years earned the increase. In our view, a plan member earns an increase in the whole pension benefit while that increase is taking place. If the member stops earning the increase, the increase will stop accruing. The increase is part of the total economic package for which the member gives employee services. The employer provides that whole economic package for current services and the hope of future services.

No one suggests that a plan member's post-division increase in salary is shareable even though length of service during the marital years helps to create the opportunity for obtaining the increase. There is no reason, in our view, to treat that part of an improvement in the member's economic package which is an increment to the pension benefit any differently from that part of the improvement that is the increase in salary, upon which the increment to the pension plan depends.

vi. Valuation for valuation and accounting: summary

For all these reasons, our present view is that

- what should be valued for valuation and accounting is the assets the spouses have at the time of sharing, and

- unless a pension-plan member has a present entitlement to a future increment to the member's pension-plan benefit, the future increment does not enter into present value and should not be taken into account on the sharing of matrimonial property by valuation and accounting.

vii. Valuation for valuation and division

In our view, post-division improvements should not be taken into account for valuation and division. The reasons that we have given for not taking post-division improvements into account for valuation and accounting apply. There is the further reason that a pension plan should not be required to pay out proportionately more for a non-member spouse's share of a pension plan than it would have to pay out to a terminating member. A payment to a terminating member will not usually require the plan to include something for the prospect of post-termination improvements in the plan.

viii. Sharing by division of proceeds

In our view, post-division improvements should not be shared under a division of proceeds. The reasons that we have given for not taking post-division improvements into account for valuation and accounting apply. Our view is that the member was not entitled to the post-division improvements at the time of the division of matrimonial property and should not have to share benefits purchased by post-division employee services.

ix. Conclusion

In our view, post-division increments in pension benefits are part of the interrelated economic package which the employer provides for the employee as the price of the employee's services for the years in which the increments occur. The post-division increments must be bought and paid for by the member through the provision of their services and often through employee contributions. Matrimonial property should be divided so that the spouses will share in the gains of the marital years. The non-member spouse should not share in pension-benefit gains which are the fruits of the member's post-division efforts, and the member should not be required to pay the non-member for benefits which the member must purchase from the plan by contributions and employment services.

We have expressed our views in firm language. We have done so in order to expose our reasoning in detail so that it may be criticized. We invite that criticism.

The question is controversial and reasonable persons may disagree about the answer. As noted, British Columbia legislation requires the use of retirement value. Legislation in Manitoba, New Brunswick, Nova Scotia and Quebec appears to exclude post-division accruals.

WE INVITE COMMENT.

> ***Question 2: Effect of death of a spouse.***
>
> ***(1) Under a division of proceeds, should the death of the non-member spouse terminate the non-member's share in the pension benefit?***
>
> ***(2) Under a division of proceeds where the non-member is sharing in a joint-and-survivor pension, should the non-member continue to be entitled to receive the same dollar amount if the death of the plan member brings about a decrease in the pension?***

Recommendations 13 to 16

This question affects Recommendations 13 to 16 of ALRI's Report 48. Again, there is a difference in approach between ALRI and the LRC BC, and out of respect for the Commission's views we think that we should discuss the subject at some length. Although the question has two distinct parts, we think it best to treat them as one subject.

ALRI Recommendations 13 and 14 would give the non-member spouse a share in death benefits under an unmatured pension benefit. Recommendation 15 would bring into the non-member spouse's share a pension paid to another beneficiary after the death of the plan member. Recommendation 16 would continue the non-member spouse's share of a pension benefit if the non-member spouse predeceases the member.

These recommendations are based on the concept of a pension benefit as "property". A pension benefit is a strange sort of property because it consists of rights against a pension plan to receive money payments that will be different under different circumstances. Nevertheless, a pension benefit consists of legal claims and rights which are properly considered to be "property" for the purpose of dividing matrimonial property on marriage breakdown. It is, in our view, something which the member has, the benefit of which should be divided, whether in specie or through the device of an equalization or compensation payment. The

accumulation of property is a process which has gone on during the marital years, and the division of that accumulation is a matter of entitlement that does not depend on needs or resources. Support, which does consider needs and resources, is, in our view, something to be considered or reconsidered after, and in the light of, the as-of-right division of matrimonial property and should not affect that division, which is a recognition of the past.

It follows that all rights which a plan member has against the plan are divisible.[14] Death benefits are divisible, including the contingent right to death benefits. Recommendation 15 of Report 48 carries this concept a long way. Under it, if the member has a joint-and-survivor pension with a later spouse, and if the member dies, the non-member ex-spouse would share in that survivor pension. Recommendation 15 is based on the property concept.

The LRC BC makes two proposals which we think express a different philosophy. They both apply where the pension benefit has matured, that is, when a pension is being paid, and when the division is by division of proceeds, or "benefit split".

Death of non-member spouse before death of the member spouse

The first of the two proposals of the LRC is that if the non-member spouse dies before the plan member, the benefits should cease with the non-member spouse's death.[15] The Commission's view is that termination "must certainly be the case where survivor benefits reduce on the death of the spouse", and that the advantages of simplicity in the scheme "even at the cost of some logical inconsistency" prevail if the benefits did not reduce on death. The text of the Report does not give the reasons for these views.

As indicated above, our approach to the question is predicated on the notion of a pension benefit as property the whole of which is to be shared. It is quite true that a non-member spouse does not have any need for a pension after their death. But the division of matrimonial property is not predicated on need, but rather on the fact that the pension is the proceeds of property that was accumulated during the marriage. The member still has a right as against the pension plan to receive whatever pension is due after the non-member spouse's death, and that right is

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[14] Different considerations apply to disability benefits paid under a pension plan, and this discussion does not apply to them.

[15] See BC Report at 49, including n. 54, the proposed s. 55.6(1) at 85 and the proposed s. 55.8(1) at 87.

part of the matrimonial property which was to be divided. And we think that the economic gain during the spouses' marriage included the whole of the pension benefit, so that any and all annuities (as well as other financial benefits paid under the plan) paid under the pension benefit are included. They will be valued for a valuation and accounting or a valuation and division, and we think that they should be included in the proceeds that are divided under division of proceeds.

We do not think that a reduction in benefits upon the non-member spouse's death affects the issue. In a case in which the member has elected to take a joint-and-survivor pension with a reduction on the death of either spouse, the remainder is still paid under and as part of the pension benefit. There is the further point, though we do not think it the decisive one, that it is likely that all annuities which the member could elect to take will have the same actuarial value, so that the provision for the reduction on the non-member spouse's death will have resulted in a total payment to the spouses during their joint lives that is greater than it would have been if there had been no reduction, so that there is really no reason to penalize the non-member spouse who has died.

Death of member spouse before non-member spouse: joint and survivor pension

The LRC BC's next proposal is that if the plan member dies and there is a consequent reduction in the pension, the amount paid to the non-member spouse must not be less than the amount paid before the reduction.[16] We take this to mean, for example, that if a pension of $10,000 which was being shared equally between the spouses drops to $6,000 on the member's death, the non-member spouse will be entitled to $5,000 and the member's estate or beneficiaries will receive $1,000. The note accompanying s. 55.8(2) says that "ordinarily, the reason for reducing the benefits is that the survivor does not need the entire original amount. A proportionate share of the reduced pension, however would leave the surviving spouse with too little", and the spouse's share should be no less.

No doubt the reason for the common provision for the reduction of a pension on the death of the first spouse to die is that, when two spouses have been living together and one dies, the needs of the survivor are likely to be less than the previous needs of the couple. But that consideration, while it may determine the form that the matrimonial property takes, does not, in our view, entitle the surviving ex-spouse to a larger share of the matrimonial property than was determined at the time of division.

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[16] BC Report, at 87, draft s. 55.8(2).

The division of pension benefits is not, in our view, support-based. The actual needs of the non-member spouse from the pension may be zero, or they may be several times what the pension provides. The share in the pension remains the same throughout. We do not see why needs should be introduced at the time of the member's death. It seems to us that the same proportionate division of the property, whether equal or otherwise, should apply throughout.

WE INVITE COMMENT.

C. Methods of Sharing

> ***Question 3: Methods of division and order of preference.***
>
> ***Subject to matters raised in Questions 4 and 5, should the five methods of division and the order of preference in Report 48 be maintained for vested pension benefits?***

1. Description of ALRI pension-division scheme

In ALRI's Report 48, we recommended that the Court have power to order any of 5 different ways of sharing a pension benefit:

- **valuation and accounting**, under which the member spouse would retain the pension benefit and compensate the non-member spouse for the latter's share. The compensation could be a cash payment, a credit in the statement of account between the spouses, or the transfer of other assets. This would require a valuation of the pension benefit.

- **valuation and division**, under which the pension plan administrator would pay out for the non-member spouse's benefit the value of the non-member spouse's share in the pension benefit. (This would normally go to an RRSP or other pension vehicle for the non-member spouse.) Devices similar to valuation and division appear to be allowed, and sometimes mandated, by post-Report 48 legislation in British Columbia, Saskatchewan, Manitoba, Quebec and New Brunswick.

- **provision of a separate pension** for the non-member spouse, under which the pension plan would provide a pension which would be of a kind provided by the plan and have the appropriate actuarial value. Similar devices appear to be allowed by post-Report 48 legislation in British

Columbia, Saskatchewan and Nova Scotia and by unproclaimed legislation in Prince Edward Island.

- **division of proceeds by the pension plan administrator**, under which the pension plan administrator would pay to the non-member spouse the appropriate share of the pension as and when paid. Some post-Report 48 legislation envisages this.

- **division of proceeds by the employee spouse**, under which the member spouse would receive the proceeds and pay over the non-member spouse's share. No special legislation is needed for this.

We went on to recommend that in dividing property, a court should consider those methods of division in that order, with some qualifications. Generally speaking, valuation and accounting would be applied unless it would lead to a result that is not just and equitable or would cause hardship. If valuation and accounting was not applied, valuation and division would be applied, subject to rejection for similar reasons, and so on.

2. Reasons for ALRI scheme of pension-division

Our reasons for adopting this order of preference were as follows:

- We thought that valuation and accounting, where it is practicable, is the best form of division because it severs the relationship of the parties with respect to the pension benefit, and this is highly desirable in the interests of efficiency, giving both spouses a firm foundation for future planning, and avoiding imposing any burden on the pension plan or its administrator.

  In particular, if the non-member spouse has the greater share of divisible property, it is unlikely that it will be to the advantage of the spouses to share the pension benefit in specie.

  There are downsides. Valuation and accounting requires a valuation of the pension benefit asset despite uncertainties about the survival of the member spouse to retirement and the length of the member's survival afterwards, the value which the pension will have when it commences, the appropriate discount rate to apply to that value, and the continued solvency of the pension plan. Valuation and accounting, if it is justice, is necessarily rough justice.

But people do rely on the present value of a future annuity in their dealings so that it is not unfair to deal with a future pension on that basis.

- Valuation and division also severs the financial relationship and gives the spouses a firm foundation for future planning. The payment made to the non-member spouse is in the context of the way in which the pension plan is valued for the purposes of its members.

  We ranked this method second because it does impose some burden on the pension plan administrator. It also effectively restricts the non-member spouse to using the proceeds for pension purposes, which may be a good thing as it helps to promote pension objectives, but which may prevent the non-member spouse from using the proceeds for some purpose that is more beneficial in the circumstances.

- We ranked the provision of a separate pension ahead of division of proceeds because
  - it also severs the financial ties between spouses, though it does not sever the pension account until the time when a pension can be claimed;
  - it gives the non-member spouse a pension tailored to the non-member's needs, so that no conflict about exercising options for early retirement or kind of pension will arise.

3. ALRI's present view

We think that ALRI's general approach as outlined above is still valid, that is, the provision of a number of ways of dividing pension benefits and the establishment of an order of preference. We will, however, take a fresh look at it, both in general and in relation to the specific order of preference, in the light of comments received on this consultation. In particular, we will set out for consideration as Questions 4 and 5 two suggestions for a different ordering of the proposed methods of division. The first is that provision of a separate pension be moved to the bottom of the list. The second is that division of proceeds by the plan member be moved ahead of division of proceeds by the plan administrator.

WE INVITE COMMENT.

Question 4: Cost and preference status of provision of a separate pension.

(1) Should "provision of a separate pension"

(a) be discouraged (with the possible exception of a case in which the member is within, say, 5 years of retirement)?

(b) be ranked after rather than before division of proceeds?

(2) Should spouses pay the actual cost of providing a separate pension, or a prescribed amount towards the cost, or should the cost be borne by the pension plan?

As noted, ALRI, in Report 48, ranked the provision of a separate pension

- **after** valuation and accounting and valuation and division, because it does not completely separate the affairs of the spouses and because of the administrative burdens it will impose on pension plans, but
- **before** division of proceeds, because of the greater degree of separation of the affairs of the spouses it provides.

We were not sure whether the provision of a separate pension would impose a greater administrative burden on pension plans than would division of proceeds by the plan administrator.

AEPPAAC has suggested that "where the employee spouse is not close to early retirement, this approach [provision of separate pension] should be discouraged where possible". The reason is the burden that will be imposed on plan administrators, who will have to keep track not only of the plan member but also the ex-spouse over a period of years and then establish a separate pension account, with all the administration involved in another set of elections and paying the non-member a pension. AEPPAAC recognizes that

> where the employee spouse is close to retirement or early retirement, perhaps within 5 years, there may be some value to this approach, so long as the pension plan is compensated for the costs of the separate pension.

This recognizes that, given the imminence of retirement, there is much to be said for avoiding the difficulties of valuation so that the practicalities of the parties have a greater weight in determining whether the provision of a separate pension is an efficient method of division, and the administrative burden, while it still exists, is less, so that it has lesser weight than at an earlier stage of the spouse's lives.

We remain of the view that the provision of a separate pension is better **for the spouses** than the division of proceeds. This is largely because:

- the two spouses can elect for different pensions, thus avoiding clashes of interests;
- the non-member spouse's pension benefit is tailored to the non-member spouse's vital statistics rather than to those of the member;
- it avoids any problems of attribution of income tax;
- it makes it unnecessary for the member to receive pension payments and pass on the non-member's share (though division of proceeds by the plan administrator will also avoid this problem).

But the provision of a separate pension is not the best **for the pension plan**. Providing the benefit to the spouses imposes a burden on the pension plan. From the time of the division of matrimonial property, the plan administrator will have to keep a record of the non-member's entitlement and keep a file on the non-member. At time of crystallization, the plan administrator will have to separate the member's account into two accounts and go through the administrative processes necessary to establish the value for plan purposes of each. The plan administrator will then have to secure elections from two "members" and set up files for the provision of two pensions instead of one. Then, every month, the administrator will have to make two payments instead of one while both ex-spouses live. If the non-member spouse outlives the member, the plan administrator will have to continue payments over a longer period than would have been required if separate pensions had not been provided.

There is thus a conflict between the two interests, the interest of the plan and the interest of the divorcing spouses. What balance should be struck? The problem—the need to divide the pension benefit on marriage breakdown—is created by the two spouses. Third parties—the plan administrators, sponsors and beneficiaries—should not suffer because of a problem created by the spouses, particularly if the cumulative administrative burdens imposed by numbers of divorcing members will tend to make the establishment of pension plans less attractive to employers. On the other hand, pension plans are for the benefit of members, and significant needs of those plan members who suffer marriage breakdowns (to which all married members are potentially subject) should be met

even if the additional administration imposes some cost on the plan and even if that cost has to be borne out of the common funds.

The LRC BC considered the question of cost to the plan. Its general view was that there would be a cost but that, if an appropriate legislative scheme is provided, the cost will decrease as the process becomes familiar. Its conclusion was that the account split should be provided, but that the member and non-member should be required to pay towards administrative costs an amount prescribed by regulation. The numbers suggested by the Commission were $400 for a pension in a defined benefit plan, $100 for a pension in a defined contribution plan, and $500 for a hybrid plan.[17] The numbers adopted by regulation are $500, $150 and $650 respectively.

We stop to note a comment by AEPPAAC:

> The wording under this section [provision of a separate pension] is not entirely clear. We presume the intent is that the principle of actuarial equivalency would be followed in determining the pension entitlement.

ALRI's intention was that the principle of actuarial equivalency be followed in determining the pension entitlement. It is a necessary principle if the integrity of the plan is to be maintained while dividing the benefit properly between the spouses. We agree with AEPPAAC on the point and all that is needed is clarification of wording.

WE INVITE COMMENT.

> ***Question 5: Preference status of division of proceeds.***
>
> ***Should the order of preference be revised by putting "division of proceeds by member" before, instead of after, "division of proceeds by plan administrator"?***

AEPPAAC has also suggested that the order of preference under ALRI's Report 48 be revised by ranking "division of proceeds by member" ahead of "division of proceeds by plan administrator".

The grounds for this proposal are similar to the grounds for AEPPAAC's proposal to move the provision of a separate pension to the last position, that is, the administrative costs and burdens that keeping track of an additional

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[17] BC Report, at 25-26 & 27-30.

"member" and dividing and sending out two payments instead of one will impose on pension plans.

The arguments against the proposal are much the same as the arguments in favour of keeping the provision of a separate pension in its original position in the order of preference. In particular, if proceeds are to be divided by the member, the non-member's timely receipt of their share is dependent on the member both receiving pension cheques and moving promptly to send on the non-member's share, which leaves the affairs of the two ex-spouses entangled.

WE INVITE COMMENT.

> ***Question 6: Application of pension benefit to equalization payment.***
>
> ***Should it be possible to apply part of the member's pension benefit as part or all of an equalization payment by***
>
> ***(a) payment of part of the value of the pension benefit into a registered pension vehicle for the non-member spouse?***
>
> ***(b) providing a separate pension or division of proceeds and applying the value to the equalization payment?***

Division at source by transfer

Essentially, valuation and division will divide a pension benefit in specie in the same proportions as the whole of the matrimonial property is divided. The division is effected by a cash payment, but the payment is a share of the value of the pension benefit. Since the pension benefit is being divided separately in specie, it will not be listed on a statement of the spouses' assets for the purpose of determining what the equalization payment will be.[18]

The OLRC has recommended that the law provide for "division at source" by transfer of money. This resembles valuation and division. However, the pension benefit, instead of being divided in specie, would be used as the source of all or part of an "equalization payment", that is, the amount that a spouse must pay in order to equalize the amount of divisible matrimonial property held by each spouse. AEPPAAC has also suggested that such a device might be worth considering. We do not see any objection in principle. We think the question is

[18] Of course, the division of property may be in other than equal shares.

whether the device would give spouses additional flexibility that would justify adding an additional complication to the scheme.[19]

An example may show the difference between the effect of valuation and division, on the one hand, and the OLRC's proposal for division at source by transfer, on the other. Suppose that the divisible matrimonial property is to be divided equally and is held by the spouses as follows:

Property		Member	Non-member
Pension benefit			
Present value	75,000		
Allowance for tax	18,750	56,250	0
Other property		40,000	0
TOTALS		96,250	0

If ALRI's preferred proposal, valuation and accounting, is used, the plan member will pay the non-member spouse $48,125, being half of the $96,250 differential. The plan member will then have a pension benefit with a present value of $56,250. All the member's other divisible property will probably have gone to make the equalization payment and the member, in addition, will have had to find another $8,125 either by borrowing or by applying non-divisible property.

If valuation and division is used for the pension benefit (possibly on the basis that it would not be just and equitable to strip the plan member of all other property and leave them with a debt), the pension benefit will not appear on the account: in the example above, only the member's other property worth $40,000 will appear. The plan member will pay the non-member spouse $20,000 in cash or property, being half of the value of the other property. The pension plan will pay $37,500, being half of the value of the pre-tax pension, into the non-member spouse's pension vehicle. Each spouse will have a tax-liable pension benefit with a present pre-tax value of $37,500 and a tax-free $20,000 in other assets.

The OLRC proposals would allow **part** of the pension benefit to be applied to the equalization account. For example, enough of the pension benefit could be used to give the plan member a $15,000 credit, allowing the plan member to pay another $33,125 and retain $6,875 in other assets, instead of making up the

[19] This should be qualified by reference to the discussion below of a 50% limit on the amount of the pension benefit that can be used.

difference by transferring or selling all divisible assets and finding some money elsewhere besides. Each spouse will then have a pension benefit and some other assets. Other permutations could be tailored to the spouses' specific situation. So, allowing the use of a pension benefit as a source of part or all of an equalization payment may provide additional flexibility. It will do so only if the plan member's share of the divisible assets is greater than the share to which the plan member is entitled, as in the reverse situation the plan member will not be required to make an equalization payment.

One question that arises is the effect of the potential liability for income tax. The question does not arise under valuation and division: the spouses share in the potential income tax liability in the same proportions as they share in the asset, and the possibility that one may ultimately pay tax at a higher rate than the other need not be taken into account. But, if the value of a pension benefit on a valuation and accounting has been adjusted to reflect a potential tax liability (as in the example given above), we think that an amount paid from the pension plan on account of an equalization payment will also have to be adjusted. To put it another way, a dollar paid on the member's behalf to the non-member's pension vehicle is not worth a whole dollar because it cannot be withdrawn from the pension system without paying tax. It appears to us that, if the pension benefit is used as a source of an equalization payment, an adjustment will have to be made for the potential tax liability.

If an adjustment is made for tax, should it be the same as the adjustment that was made to arrive at the value charged to the member spouse on the valuation and accounting? We think that it should, but we note that an argument can be made that the adjustment should be based on the **non-member spouse's** prospective tax rate rather than the **member** spouse's prospective tax rate which would have been used in order to get the value for the equalization statement.

If part of the pension benefit is to be transferred out of a pension plan for payment of an equalization obligation, we think that the amount available should be limited to 50%, as the OLRC proposes and legislation in some provinces provides, as well as the federal PBSA.[20] If the whole pension benefit could be used, the member would not, immediately following the division of matrimonial property, have any deferred pension, and this seems wrong in principle.

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[20] See the Ontario Report, at 177, for a list of legislation. The 50% would be based on "termination" value.

Benefit splits

The OLRC also proposes a form of division of a pension by a "benefit split". This would provide the non-member spouse a separate pension. If the pension benefit has not matured at division time, the pension would be deferred. If the pension benefit has matured, the pension would be immediate. Presumably the present value of the deferred or immediate pension would be applied to the equalization payment. Again, we would think that an adjustment would have to be made for tax liability. Should such a provision be made in Alberta?

WE INVITE COMMENT.

> ***Question 7: Minimization of cost and intrusion.***
>
> ***(1) Should Recommendation 1 of Report 48 be varied by adding an additional consideration to be borne in mind in applying the principles stated in the recommendation, namely, that costs to the pension plan should be minimized?. (Costs include administrative time, costs of consultation and communication with the employee and employee spouse and their advisors, etc.)***
>
> ***(2) Should the principles include the idea that the intrusion by third parties into the private lives of the employee and non-employee spouse should be as minimal as possible.***

AEPPAAC suggest that these variations should be made.

We agree with item (1). We think that it is included in Recommendation 1(3) of ALRI's Report 48, which reads as follows:

> (3) that the rights of third parties should not be prejudiced by the division of a pension benefit between the spouses.

However, in order to achieve greater clarity we will vary Recommendation 1 as AEPPAAC proposes. The principle will have to be balanced against the principles of fairness and equity as between spouses: see the discussion of Questions 4 and 5 above.

We would agree with item (2) if the standard were "as minimal as **practicable**, having regard to the interests of the spouses". That is, the principle of non-intrusiveness is for the benefit of the spouses and should not stand in the way of having third-party intrusion through division of proceeds by the pension

plan or the provision of a separate pension if that is in the interest of the spouses.[21]

WE INVITE COMMENT.

D. Specific Questions About Valuation and Division

> ***Question 8: Time of valuation and division.***
>
> ***Should "valuation and division" occur at the time of division of matrimonial property or at or after the first time at which the member could take a pension?***

Outline of LRC BC proposal

The LRC BC[22] has raised an important question about valuation and division: should it take place at the time of the division of matrimonial property, or should it take place at a later date?

ALRI's Report 48 recommended that valuation and division take place at the time of the division of matrimonial property. However, with respect to defined benefit plans, the LRC BC report recommends

- that the non-member spouse be entitled to elect to have the pension benefit divided by the Commission's counterpart of valuation and division, but
- that the non-member spouse cannot make the election until the member becomes entitled to retire under the pension plan.[23]

Under the LRC BC proposal, "termination" value would be used (rather than the "retirement" value which, under the LRC BC proposals would be used for a valuation and accounting). It would, however, be "termination value" as at the time of the election, including post-division improvements that take place in the pension benefit up to the time of the election.

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[21] Subject, of course, to the discussion above as to whether any option will impose too much administrative burden on a pension plans.

[22] BC Report, at 37-38.

[23] BC Report, at 82, draft s. 55.5.

Theoretical justification for proposal

The LRC BC gives the following theoretical justification for postponing a valuation and division:[24]

> The theoretical structure of this model is that the spouse has a continuing property interest in the member's pension. Consequently, there is no reason why the spouse cannot wait to have the share paid out.

The Family Relations Act (B.C.) does provide, in s. 43, that, upon the happening of a triggering event, each spouse has an undivided half interest as tenant in common in all family assets, which include pension benefits. This is presumably the basis of the reference to a continuing property interest in the passage quoted above. However, s. 7(1) of the Matrimonial Property Act (Alberta) merely provides that the Queen's Bench "may ... make a distribution between the spouses of all the property owned by both spouses and each of them", subject to a number of exceptions, so that there is no "continuing property interest": that is to say, the MPA does not confer a continuing property interest. That seems to make the theoretical basis of the LRC BC's proposal inapplicable in Alberta. However, whatever the statute says, it seems to us that the purpose of the operation should be to divide property so that one spouse will have sole ownership of each asset with no continuing property interest held by the other spouse: a situation in which each spouse has a continuing property interest in the same asset should be allowed to exist only if there is no satisfactory alternative way of sharing the benefits of the asset.

Effect of proposal on pension plans

The LRC BC is of the view that the proposal to postpone valuation and division will not prejudice pension plans because there is no guesswork involved in the calculation.[25] We agree that, statistically speaking, paying out a share of a pension benefit at a later rather than an earlier date should not cause a loss to a pension plan, as, in each case, the plan would be paying out a share of the present value of the benefit and would be liable for providing a pension based on the remaining share, so that its liabilities should track its resources. (This assumes that the present value of the member's residue will not exceed the pre-division present value less the amount paid out for the non-member spouse.)

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[24] BC Report, at 38, footnote 39.

[25] *Id.*

The proposal does, however, raise the question whether the administrative burden of keeping track of non-member spouses should be imposed on pension plans in addition to the burden of making calculations of present value and paying out non-member spouses' shares. We would appreciate specific comment about the effect such a proposal would have on pension plans.

Effect of proposal as between the spouses

The postponement of the valuation of the pension benefit to the earliest retirement date would give a non-member spouse the benefit of all increases in the value of the pension benefit up to the date of the election, including increases due to plan improvements and increases due to increased earnings of the plan member. For the reasons we have given above,[26] we do not think that a non-member spouse should be given an entitlement to the benefit of post-division increases in the value of a pension benefit.

We are advised that, at least in some cases, a pension plan will, when determining the amount of pension to be paid after a valuation and division, deduct from the plan member's pension the amount of pension represented by the amount paid out under the valuation and division. In such a case, under the hypothetical example set out at pages 6-7,

a) the pension plan would, at the time of division of the matrimonial property, pay out the commuted value of a deferred pension of $3,000, being half of the $6,000 deferred pension to which the member was entitled at the time of division for 10 years' pensionable service (subject to survival to retirement age);

b) the pension plan would, at the time of retirement, provide the plan member with a pension of $13,000, being the pension of $16,000 to which the plan member would have been entitled for 20 years' pensionable service, less the $3,000 the commuted value of which was paid out on the valuation and division.

If valuation and division were deferred to retirement time, the non-member spouse's share would be 50% (being the spouse's share) of one half of the $8,000 of pension then attributable to the marital years, or $4,000 of pension, leaving the plan member with $12,000 of pension instead of $13,000. This flows from the postponement of valuation and division, as the postponement gives the spouse the

[26] See the discussion at pages 6 to 16 above.

benefit of the post-division increments to the pension benefit up to the time of the election.

Conclusion

The LRC BC proposal for the deferment of valuation and division raises some difficult and complex issues. We would appreciate any assistance that can be given in understanding and evaluating them.

WE INVITE COMMENT.

> ***Question 9: Restrictions on payments from pension plans for valuation and division.***
>
> ***Should***
>
> ***(a) the provisions of the EPPA relating to when payment of commuted values may not be made apply to a valuation and division on division of matrimonial property?***
>
> ***(b) the certificate an actuarial report attesting to a solvency deficiency in a pension plan be conclusive?***

Recommendation 9 of ALRI's Report 48 read as follows:

> We recommend that the certificate of a pension plan administrator that a valuation and division of an employee spouse's pension benefit would prejudice the liquidity or the solvency of the pension fund be proof of the truth of its contents in the absence of evidence to the contrary and that it not be overridden unless the pension plan administrator has been given notice of an application for that purpose and has had an opportunity to give evidence and be heard.

AEPPAAC suggests that, in the case of plans regulated under the EPPA, the provisions of that Act as to the payment of commuted values on termination should apply with respect to the division of pension benefits on marriage breakdown. This appears appropriate, given the similarity of circumstances.

AEPPAAC also suggests that an actuarial report attesting to a solvency deficiency should never be overridden. We are inclined to agree that when it comes to a possible insolvency, this is appropriate.

It will be noted that valuation and division is not likely to be just and equitable if there is any restriction which prevents the payment out of a pension fund of the whole value or proceeds of a pension benefit. If, for example, only contributions and interest can be paid out, valuation and division may not be appropriate.

WE INVITE COMMENT.

Question 10: Income tax consequences of valuation and division.

(1) Will valuation and division attract adverse income tax consequences if the non-member spouse's share is paid into a registered pension vehicle?

(2) Should the law require non-member's share under a valuation and division to be locked-in?

Contributions to registered pension plans are deductible from income by employers and employees, and increments to the value of pension benefits are not taxable as they accrue. However, benefits paid out by pension plans **are** taxable when they are paid, without any deduction for the contributions. The effect of registering pension plans is thus to defer tax, not avoid it, and to make it payable by the recipient.

If an amount paid by a pension plan for the benefit of a non-member spouse under a valuation and division were to be added to the income of either spouse in the year in which the payment is made, the payment of tax would be accelerated, and in many cases the tax would be at a high marginal rate. It is therefore of importance to know whether or not that acceleration will take place.

ALRI's Report 48 discussed the tax situation. Essentially, it said that our tax advice, while not based on absolute legal bedrock, was that a valuation and division under which the non-member spouse's share was rolled over into a new registered pension vehicle, would not accelerate tax. That was in 1986. Section 60(j) of the Income Tax Act, upon which that advice was predicated, has since been amended and no longer protects payments from registered pension plans.

However, s. 147.3(5) and (9) of the ITA read as follows:

> **(5) Transfer to RPP, RRSP or RRIF for spouse on marriage breakdown.**—An amount is transferred from a registered pension plan in accordance with this subsection if the amount
>
> (a) is a single amount;
>
> (b) is transferred on behalf of an individual who is a spouse or former spouse of a member of the plan and who is entitled to the amount under a decree, order or judgment of a competent tribunal, or under a written agreement, relating to a division of property between the member and the individual in settlement of rights arising out of, or on a breakdown of, their marriage; and
>
> (c) is transferred directly to
>
> (i) another registered pension plan for the benefit of the individual,

(ii) a registered retirement savings plan under which the individual is the annuitant (within the meaning assigned by subsection 146(1)), or
(iii) a registered retirement income fund under which the individual is the annuitant (within the meaning assigned by subsection 146.3(1)).

(9) Taxation of amount transferred.—Where an amount is transferred in accordance with any of subsections (1) to (8),

(a) the amount shall not, by reason only of that transfer, be included by reason of subparagraph 56(1)(a)(i) in computing the income of any taxpayer; and

(b) no deduction may be made under any provision of this Act in respect of the amount in computing the income of any taxpayer.

A valuation and division, if the payment is made directly to an RPP, RRSP or RRIF[27] in the non-member spouse's name, appears to be protected by s. 147.3(9) from being included in the income of either spouse for the year in which the payment is made. While s. 147.3(9) gives protection only against s. 56(1)(a)(i), our understanding, based on an informal discussion with an official, is that there is no other provision in the ITA which would bring the payment into income. We are seeking an official statement from Revenue Canada in order to ensure that our understanding is correct.[28] We would appreciate any further information or views about tax that any reader can give us.

In Report 48, we did not recommend that there be a legal requirement that the non-member spouse's share on a valuation and division be paid into a locked-in pension vehicle. That appeared to us at the time to be a matter of pension policy rather than a matter of the policy relating to the division of matrimonial property. AEPPAAC suggests that the transfer of pension entitlements should be to an RRSP, LIRA, LIF, or LRIF and should be locked in for pension purposes. Upon further reflection, we are inclined to agree. The division of matrimonial property should not be a means of subverting either pension policy or tax policy. Anyway, a transfer to anything but one of the recognized pension vehicles would be likely to accelerate tax and neither spouse is likely to want that to happen.

WE INVITE COMMENT.

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[27] The protection of s. 147.3(9) appears to be restricted to transfers to RPPs, RRSPs and RRIFs. It does not appear to extend to other pension vehicles.

[28] Some provisions of the regulations dealing with conditions of registration of pension plans, though they may not be directly relevant, tend to confirm that payments out of pension plans in connection with the division of matrimonial property are permissible: see Regs. 8501(1),(5); 8502(c)(iv); 8503(3). Regulation 8503(3) may be important: it contemplates that payments may be made to non-member spouses on marriage breakdown but requires as a condition of benefits for a spouse or former spouse that total present value of the benefits after the payment must not exceed the present value of the benefit as it stood before the payment.

E. Specific Questions About Division of Proceeds

> ***Question 11: Elections where proceeds are divided.***
>
> ***Where the proceeds of a deferred pension are to be divided how should elections under the pension plan be made?***

Recommendation 12 of ALRI's Report 48 was that a plan member should be able to make elections only with the non-member spouse's agreement or court order, but that if the election relates to the member's employment the court should give its approval unless the non-member spouse is not acting in good faith. Our reason for requiring consent or court approval was basically that the interests of the two spouses may come into conflict and that something should be done to resolve the conflict. Our reason for requiring the court to give approval if the election relates to employment—e.g., retirement date—and is made in good faith is that the plan member, in our view, should not have to continue to work or stop working in order to advance the interests of the non-employee spouse and should not, as some plan members have been required to do, have to pay the non-employee a share of a pension that the employee spouse is not receiving.

Essentially, Recommendation 12 would leave the choice among the retirement dates permitted by a pension plan under the control of the member unless bad faith can be shown, but would require either party agreement or court order for other elections, principally elections among the various pensions provided by the plan in question.

AEPPAAC has expressed concerns about Recommendation 12 because the recommendation requires either continuing contact between, and common decisions by, two former spouses whose affairs should be separated if possible, or alternatively going to court, with all the cost, delay and bitterness involved. We agree that these are legitimate concerns. We also agree with AEPPAAC when it says that these problems are part of the reason for encouraging payout from the pension plan if the pension has not yet commenced.

However, we are dealing here with cases in which, for some reason or another, at least one party does not want to proceed by way of payout by the member or by the plan and in which the Court does not consider it just and equitable to require the parties to do so. (Under our proposals, division of proceeds comes after provision of a separate pension in the preference list, but, as noted

above, AEPPAAC's proposal is that the provision of a separate pension should go to the end of the line.)

If a case arises in which all otherwise preferable methods of division have been ruled out by the circumstances of the specific case, something has to be done about the difficult problem of elections. The only ways to avoid either further agreement or court application that we can think of would be:

- give one spouse (probably, though not necessarily, the member spouse) power to make the elections;
- delegate to someone (probably, though not necessarily, the plan administrator) the power to make the elections; or
- prescribe by legislation what elections should be made.

None of these seems to us to be satisfactory. The consequences of any other way of dealing with the question that we can think of seem to us to be likely to be worse than the undoubtedly unfortunate consequences of Recommendation 12.

WE INVITE COMMENT.

F. Valuation

Question 12: Valuation of vested pension benefits.

(1) How should a) a pension benefit, and b) the residue of a pension benefit after payment of a sum of money out of the pension plan be valued?

(2) In particular,

(a) should different standards of value be applied in valuation and accounting and in valuation and division?

(b) should the use of the CIA Standard of Practice be mandated for a valuation and accounting?

(c) should the use of the CIA Transfer Recommendations be mandated for a valuation and division?

(d) is it appropriate to take into account the prospect of non-contractual indexing in a valuation and accounting?

(e) should the law, by regulation or otherwise, say something about the valuation of the plan member's remaining share?

(f) should the legislation say anything about how and when an adjustment for income tax liability is to be made?

1. General discussion

It will be necessary to value all or part of a pension benefit for the following purposes:

- **Valuation and accounting.** It will be necessary to determine the value of the member's pension benefit in order to determine how much the member must pay to the non-member or credit the non-member with.
- **Valuation and division.** It will be necessary to determine
  - the value of the member's pension benefit in order to determine how much the pension plan must pay out to or for the benefit of the non-member spouse.
  - the value of the member's remaining interest. (We are not sure whether the valuation must be in money terms, in terms of a reduced amount of deferred pension, or simply as a fraction of the rights the member had before the valuation and division. We invite comment on this point.)

- **Provision of a separate pension.** Will it be necessary to value the pension for this purpose? It appears to us that it is likely that it will be necessary, as the non-member spouse will have elections to make, and in order to determine relative actuarial values, it may be necessary to know the present value.

In Report 48, ALRI, apart from references to adjustments for prospective income tax liability, did not propose any specific valuation methods. What it did do, through Recommendation 24, was to recommend that regulations be promulgated annually adopting interest and discount rates for deferred annuities and tables of values for such annuities.

The situation has changed materially since Report 48 was issued:

- Pensions are now "portable" and provision has to be made to value them for that purpose.
- S. 23(1) of the Employment Pension Plans Regulation provides in effect that, for the purposes of the EPPA, actuarial present value of benefits is to be determined "in accordance with the recommendations for the computation of transfer values of pensions issued by the Canadian Institute of Actuaries, as amended from time to time".
- The Canadian Institute of Actuaries ("CIA") has issued two sets of valuation standards:
  - *Recommendations For The Computation of Transfer Values from Registered Pension Plans* (which is the current version of the recommendations referred to in s. 23(1));
  - *Standard of Practice for the Computation of the Capitalized Value of Pension Entitlements on Marriage Breakdown for the Purposes of Lump-Sum Equalization Payments.*

We will discuss the situation in light of these changes.

2. Valuation of pension benefits for valuation and accounting

The CIA's *Standard of Practice for the Computation of the Capitalized Value of Pension Entitlements on Marriage Breakdown for the Purposes of Lump-Sum Equalization Payments* became effective on September 1, 1993. It provides for the valuation of pension benefits for the limited purpose described in its title, that is,

using the terminology of ALRI's proposed scheme, for the purpose of valuation and accounting. Its underlying principle

> is that the reported present value shall be determined in a manner which is equitable to both the plan member and the plan member's spouse,

and it states that

> this consideration may require the use of actuarial methods and assumptions different from those employed in determining the present values of pension entitlements for other purposes, including ... transfer values.[29]

The *Standard of Practice* provides for two methods of valuation without expressing a preference between them. One is the "termination" method, under which future salary increases are disregarded. The other is the "retirement" method, under which assumed salary increases are reflected.[30] Given the views about the sharing of post-division increments which we have expressed above, we think that the "termination" method should apply.

The *Standard of Practice*[31] provides that, where a plan does not provide contractual indexing,

> the actuary must attempt to ascertain whether the plan sponsor has established a regular and repeated practice of providing periodic pension increases on an *ad hoc* basis,

and goes on:

> Where such increases are known to have been provided in the past, the valuation must make provision for the continuation of this practice, unless there is significant evidence to the contrary (e.g., pension agreement excludes indexing where it has previously been included).

Is this appropriate? The argument against the proposition is that there is no legal assurance that the employer will voluntarily provide retired employees with enriched pensions, particularly if the member is far from retirement. The argument in favour of the proposition is that, at the time of division, the member has an expectation which is well founded, even if not founded on legal bedrock, that the improvements will continue to be made. Such an expectation is a positive element of present value despite the lack of a legal guarantee that the improvements will be made.

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[29] Ontario Report at 302 [*Standard*, p.3].

[30] *Id.*; and Ontario Report at 303 [*Standard*, p.4].

[31] Ontario Report at 312-13 [*Standard,* p.9].

The *Standard of Practice* does not provide for the inclusion of the prospect of other improvements in plan benefits in the valuation.

3. Valuation of pension benefits for valuation and division

As noted above, portability of pensions has become the rule since ALRI's Report 48 was issued, and regulations require the valuation for transfer purposes according to "the recommendations for the computation of transfer values for pensions issued by the Canadian Institute of Actuaries, as amended from time to time".[32] The CIA's recommendations are now found in its *Recommendations for the Computation of Transfer Values from Registered Pension Plans* which came into effect on September 1, 1993. These Recommendations are specifically intended to apply on a transfer to a member's pension vehicle on termination of membership. They are also intended to apply

> to the determination of a lump sum payment from the pension plan in lieu of an immediate or deferred pension to which a plan member's former spouse is entitled after an assignment of the member's pension has been made as a result of divorce, marriage annulment, legal separation or court order.[33]

They require that a transfer value "reflect the plan member's full benefit entitlement as a deferred or immediate pensioner, as may be applicable, determined under the terms of the pension plan", and that the value reflect the death benefit that would have applied before the commencement of a deferred pension plan.[34]

It seems to us that the valuation of pensions for valuation and division should be the same as the valuation of pensions for transfer for two reasons:

- what a plan member can take away at a given time is a measure of the value of the entitlement;
- standards of valuation that are fair as between the member and the plan on a transfer on termination of membership will be fair as between the member and the plan on what amounts to a partial termination.

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[32] Essentially, EPPA s. 30 authorizes a member who has a vested right to a pension, and in the case of a defined benefit pension is more than 10 years from pensionable age, to transfer the "commuted value" of the pension. Under s. 23 of Regulation 234/86, the "commuted value" is to be determined according to the CIA Recommendations.

[33] Ontario Report at 320 [*Recommendations*, p.2].

[34] Ontario Report at 321 [*Recommendations*, p.4].

The EPPA itself lays down some rules as to what must be paid out, and the CIA's recommendations will be read subject to them.

It should be noted that the CIA standard of value is what is known as a "termination" standard: it does not take into account, and therefore does not provide for the sharing of, post-division increments in the pension benefit. This is, of course, consistent with our recommendation that post-division increments not be considered unless the member, at the time of division, had an entitlement to have them made. If post-division increments were to be taken into account, this standard of value would not be appropriate.

The CIA's *Recommendations* do not go on to say how the residue of the pension benefit left in the member's hands after the valuation and division is to be dealt with. In principle, the member would have what is left of the benefit remaining after deduction of the value that was paid to the non-member. The specific form of application was left by Report 48 to be determined by regulation, with the suggestion that the regulation provide that the reduction be made by the pension plan administrator on the advice of an actuary. This raises a question: should something further be said in the legislation or the regulations about how a pension plan should deal with the residue of the pension benefit after valuation and division?

A paper entitled *Division of Pension Benefits on Marriage Breakdown* dated October 1994 and prepared by the Pension Benefits Branch, Saskatchewan Justice, paragraph 25, makes the following points that are relevant here:

1) The "sum of the value of the divided pension benefits cannot exceed the value of the pension benefits as a whole" (because that would cause the other beneficiaries of the plan to suffer), but the plan cannot take advantage of the member in the recalculation, so that the result must be cost-neutral.

   This appears to be correct in principle. Furthermore, Regulation 8503(3)(l) under the Income Tax Act applies a condition to the splitting of pension benefits on marriage breakdown: the total present value of the pension benefits held by the two spouses after the split must not be greater than the present value of the pension benefit that was held by the plan member before the split.

2) Under a contributory plan, a member's contribution account will have to be adjusted even if the plan is a defined benefit plan. Otherwise the member might receive benefits to which they are not entitled.

3) However, "the member's credited service should not be reduced for purposes of determining whether or not the member qualifies for the payment of benefits, for example, subsidized early retirement benefits based on age and service".

4. Adjustment of valuation for potential income tax liability[35]

a. Valuation and accounting

Recommendation 33 of Report 48 was that, upon a valuation and accounting, a deduction be made for the potential effect of income tax.We doubt that there is any serious argument to the contrary in a case in which the other divisible assets are not subject to a tax liability.

Report 48 did not go on to make any recommendation about how the amount of the deduction should be arrived at, and there is room for dispute as to how to determine the amount of the adjustment. What income tax will actually be paid depends on what the plan member's taxable income and income tax rates will be at the time money is paid out to the member in the form of a pension or other benefit. Complaints have been made about the use in the computation of both the member's expected marginal rate and the member's expected average rate.

The CIA *Standard of Practice for Marriage Breakdown Computations*[36] deals with the question. Essentially, it suggests that

- no allowance should be made if the value of the pension benefit will be offset by another similar pre-tax asset (e.g., a pension benefit of the non-member spouse) or will be satisfied by the transfer of a pre-tax asset (e.g., an RRSP of the member).
- where it applies, the allowance should "be based upon the member's anticipated retirement income computed in 'current' dollars" and the rate applied should be the "average tax rate paid at the most recent date ... by

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[35] See also the discussion of the effect of income tax if a pension benefit is used as part of an equalization payment at page 27 above.

[36] Ontario Report at 313-14 [*Standard*, p.10].

a similar single retired taxpayer with specified deductions ... unless applicable case law in the jurisdiction requires a different treatment".

This involves a forecast of the plan member's retirement income and assumes that tax rates and permissible deductions will be the same at and after the member's retirement as they are at the time of valuation. It adopts the **average** rather than the **marginal** rate, which results in a lower discount and a higher present value.

The result is necessarily inexact. However, the CIA approach seems reasonable. Should the legislation provide for the application of CIA standards insofar as they relate to an allowance for potential income tax liability in valuing a pension benefit for valuation and accounting?

b. Valuation and division

In Report 48, we recommended against making any allowance for tax on a valuation and division, on the grounds that each spouse will have a tax liability for proceeds of their respective shares of the pension benefit. It would be possible to argue that a differential allowance should be made if there is a significant difference between the likely tax rates that will be applied to the spouses at retirement time, but we do not think that that argument should prevail.

WE INVITE COMMENT.

5. Establishment of interest and discount rates

The CIA's *Standard of Practice for Marriage Breakdown Computations* prescribes economic assumptions for the valuation of pension benefits for valuation and accounting purposes. The CIA's *Recommendations for the Computation of Transfer Values* prescribe economic assumptions for valuation for transfer purposes, which we think generally appropriate for valuation and division.[37] The *Standard of Practice* prescribes different standards for pre- and post-September 1, 1993 marriage breakdowns, that being the date on which the standard came into force. Both the pre- and post-September 1, 1993, standards use long-term Government of Canada bonds (CANSIM series B14013), subject to certain adjustments, as the basis for determining the interest rate for the first 15 years from the valuation date for non-indexed pensions, with a rate of 6% thereafter. Both use the real rate

[37] We do not think that this is the place for a technical examination of the CIA's proposals, which fall within actuaries' area of expertise. A reader who wants more detailed information than the rough summary given in the text should refer to the two CIA documents, the relevant passages from which are reproduced in the Ontario Report at 309-11 & 324-26.

on long-term Government of Canada real return bonds, subject to adjustments, as the basis for determining the interest rate for fully-indexed pensions, with a rate of 3.00% thereafter for pre-September 1 1993 lump sum purposes and 3.25% in other cases. Actuaries are to develop appropriate interest rates for partially-indexed pensions.

In Recommendation 24 of ALRI's Report 48, we recommended that interest and discount rates be adopted annually by regulation for the valuation of deferred pensions and that tables of values be provided. AEPPAAC thinks that the CIA standards should be referred to instead. We agree.

We think that the CIA standard for lump sum computations and transfer recommendations serve the purpose that we had in mind, and, if so, Recommendation 24 of Report 48 may be withdrawn. We are strengthened in this view by the fact that the transfer recommendation is adopted by regulation. For valuation and division, it would not make sense to have a different interest rate established for essentially the same purpose as the transfer recommendation, and, as we have indicated, we think that what the plan member could transfer determines what can be transferred to the non-employee spouse. The determination of an appropriate interest rate is a technical matter that should be left to the professionals, acting reasonably.

WE INVITE COMMENT.

Question 13: Valuation of non-vested pension benefits.
How should a pension benefit be valued before vesting?

An employee who has not yet acquired a vested right to a deferred pension is likely to have no present right against the pension plan except a right to reimbursement of the employee's contributions, if any, plus interest. Recommendation 18(1) of ALRI's Report 48 was that an unvested pension benefit be valued by valuation and accounting and Recommendation 21 was that the value, subject to an adjustment for tax liability, be the amount which the employee spouse would at the time of division of the matrimonial property be entitled to receive if his employment would be terminated at that time, which would frequently be the employee's contributions, if any, plus interest.

Since Report 48, the LRC BC has recommended that the non-employee spouse have two options.[38] The first is to postpone valuation until it is seen whether or not the pension vests. The second is to have the pension benefit valued as if vested but with a discount for the possibility that it might not vest. The OLRC has recommended in favour of the second option, though without a discount if twenty-four month vesting applies and subject to a provision that the minimum valuation should be the member's contributions plus interest.[39]

Allowing the non-member spouse to share in employers' contributions made during the marital years is not the same as allowing the non-member spouse to share in plan improvements and increases in the pension benefit due to the member's increased post-division earnings. Indeed, our secondary recommendation in Report 48 was that if valuation and accounting of an unvested benefit as recommended in the report would not be just and equitable because of undue delay in vesting, the pension benefit should be divided by division of proceeds.

It is true here, as in the case of post-division increases in the value of the pension benefit, that the plan member must continue in employment and render employment services until vesting time. However, the balance of the arguments pro and con is different because what is involved is a benefit paid for during the marital years and conditional only on continued employment for what is usually a comparatively short period of time.[40] So we are in some doubt about our previous recommendation.

WE INVITE COMMENT.

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[38] BC Report at 106, Draft Reg. 13.

[39] Ontario Report at 113-14.

[40] It is perhaps worth noting that the Supreme Court of Canada, in *Strang v. Strang* [1992] 2 S.C.R. 114 says that dividing the husband's contributions was an inaccurate method of valuing a future asset and said that there were other methods available. However, it is not clear from the law reports whether the pension was unvested at the time of the division of matrimonial property, and the method of division was not an issue in the case, which was about maintenance.

Question 14: Allocation of value between marital and pre-marital years.

How should the value of a pension benefit be apportioned between pensionable service before marriage and pensionable service during marriage?

Assets acquired before marriage are exempted from division under the Matrimonial Property Act. Where a plan member's pensionable service is rendered partly before marriage and partly during marriage it is necessary to allocate the pension benefit between the two periods. Market value, which is the MPA's usual test, does not apply as a pension benefit cannot be sold. Our recommendation in Report 48 was that the value of the pension benefit be prorated according to the duration of the respective pre-marital and marital periods.

The CIA's *Standard of Practice for Marriage Breakdown Computations* sets out three possible methods of allocation without choosing among them:[41]

> At valuation date #1 (e.g., marriage), the plan member had 10 years pensionable service, had accrued $2,000 of annual pension entitlements, which at that date had a value of $5,000. At valuation date #2 (e.g., separation), the plan member had 25 years pensionable service, had accrued $30,000 of annual pension entitlements, which at that date had a value of $240,000.
>
> There are three possible approaches to addressing a member's pension entitlement acquired during marriage. One approach is sometimes referred to as "value added". Such approach develops the pension asset acquired during marriage as follows:
>
> $240,000 - $5,000 = $235,000
>
> A second approach is sometimes referred to as *pro rata* (on benefits). Such approach develops the pension asset acquired during marriage as follows:
>
> $\frac{(30,000 - \$2,000)}{\$30,000} * \$240,000 = \$224,000$
>
> A third approach is sometimes referred to as *pro rata* (on service). Such approach develops the pension asset acquired during marriage as follows:
>
> $\frac{(25 - 10)}{25} * \$240,000 = \$144,000$

ALRI's Recommendation 30 was for the *pro rata* (on service) approach. Both the LRC BC[42] and the OLRC[43] made similar recommendations, though the

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[41] Ontario Report at 303 [*Standard*, p.4].

[42] BC Report at 96, Draft Reg. 2.

OLRC thought that this approach would not be suitable for some pension plans, such as career earnings plans. The OLRC was of the view that the value-added approach does not recognize the years-of-service aspect of defined benefit plans and would be more difficult to apply as it requires information that may no longer be available.

We raise this question for review as it is a rather difficult and complex one.

WE INVITE COMMENT.

> ***Question 15: Allowance for pre-pension death of member and insolvency of plan.***
>
> ***In the valuation of a pension benefit for valuation and accounting or valuation and division, should an allowance be made for***
>
> ***(a) the possibility that the employee spouse will not live until the commencement of a pension, or***
>
> ***(b) the possibility that the pension fund may not be sufficient to pay all pensions charged upon it?***

Recommendations 31 and 32 of ALRI's Report 48 were that

- on a valuation and division no allowance should be made for these possibilities, and
- on a valuation and accounting no allowance should be made unless a valuation without such an allowance would not be just and equitable (e.g., the plan member is in bad health or the pension plan's solvency is doubtful).

Our reason for not making any allowance for the possibilities was that any increase in abstract justice which would result from allowing for either contingency "would be delusive and would be outweighed in importance by the additional complexities and cost involved in allowing for them".

Since the time of Report 48, the CIA has recommended the application of demographic assumptions about mortality. Both the CIA *Standard of Practice for*

[43] Ontario Report at 147-49.

Marriage Breakdown Computations[44] and the CIA *Recommendations for the Computation of Transfer Values from Registered Pension Plans*[45] so provide. It appears that Recommendations 31 and 32 of Report 48 should be revised to provide that the possibility of the member's death be taken into account in either a valuation and accounting or a valuation and division in accordance with the relevant CIA standard.

The CIA *Standard of Practice*[46] also deals with plan funding for valuation and accounting:

> The reported value should not be reduced on account of the pension plan not being fully funded. If the actuary is aware of extraordinary circumstances wherein the pension plan has defaulted or may reasonably be expected to default upon pension promises or expectations, the actuary should disclose such awareness, and may suggest an appropriate reduction.

Thus, if there is a doubt about the solvency of the plan, the *Standard* would leave it to the actuary to "suggest an appropriate reduction", while ALRI's Recommendation 32 would leave it to the court to determine whether the doubt would mean that valuation and accounting would not be just and equitable and should not be applied. We are inclined to think that if there is significant doubt about the plan's solvency, absent agreement of the spouses, the court should not impose valuation and accounting at all rather than make an allowance for the possibility of insolvency. That would suggest that Recommendation 32 should be retained. However, we would appreciate receiving views on the point.

The situation is different for valuation and division. The CIA transfer value recommendations say this:

> The transfer value computed by the application of these recommendations is independent of the financial position of the pension plan. Applicable legislation or the plan provisions may attach conditions to the payment of a portion of the transfer value when the plan is less than fully funded on a plan termination basis.[47]

Essentially this says that the protection of the pension plan against paying out full value for a non-member spouse at a time when its ability to meet all claims is in doubt can be left to legislation and plan provisions. If so, no change is required in Recommendation 31. But we ask: should the pension-division legislation

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[44] Ontario Report at 306 [*Standard*, pp.5,6].

[45] Ontario Report at 322-23 [*Standard*, p.6].

[46] Ontario Report at 303 [*Standard*, p.4].

[47] Ontario Report at 321 [*Recommendations*, p.4].

specifically declare itself subordinate to a) protective legislation and regulations or b) protective plan provisions?

WE INVITE COMMENT.

G. Procedure

> ***Question 16: Necessity of court order.***
>
> ***Should valuation and division, provision of a separate pension or division of proceeds by plan administrator be available to the parties without a court order?***

Under the recommendations in ALRI's Report 48, a court order would be necessary for valuation and division, provision of a separate pension or division of proceeds by plan administrator. The spouses would not be able to arrange for any of these without a court order. We intended this requirement for the protection of pension plans, thinking that they should not have to engage in these processes without the protection of a court order.

However, it seems that we were unnecessarily cautious. Both the British Columbia and Ontario Reports would allow the parties to activate the kinds of division mechanisms contemplated by those reports, and some legislation does so now. Unless comment supports our Report 48 position, we will recommend that a plan member and non-member spouse can, upon marriage breakdown, initiate proceedings to require the plan administrator to effect the division agreed upon, whether by valuation and division, provision of separate pension or division of proceeds by plan administrator. Appropriate administrative provisions would have to be made, probably by regulation, so that plan administrators would always know what they are supposed to do. Provision would also have to be made to protect the integrity of pension plans.

WE INVITE COMMENT.

Question 17: Information.

(1) What information should pension plans provide?

(2) Who should bear the cost?

(3) Should the subject be dealt with by the legislation or by regulations?

Plan members and their spouses cannot make proper agreements for the division of pension benefits without enough information to determine their values. Nor can courts make proper order for division without such information. Adequate information is therefore crucial.

In Report 48 we recommended that regulations be adopted

> requiring a pension plan administrator, upon requisition by a spouse involved in negotiating or litigating the division of matrimonial property upon marriage breakdown, or upon an order of the Court, to provide in prescribed form the information necessary to determine the present value of the employee's normal retirement annuity.

Our view was that, although important, the precise nature of the information to be provided and its precise form are better prescribed by regulation and can better be dealt with at the implementation stage than by the legislation itself.

AEPPAAC says this:

> With respect to the requirement that the pension plan administrator provide information, there should be (1) limits to the amount of such information that must be provided by the pension plan administrator and (2) the administrator should be able to recover reasonable costs associated with provision of that information. The administrator should not be required to provide a present value amount other than that which otherwise would be provided if the employee spouse had been terminated. This would ensure that the administrator would not be obliged to participate in court discussions of the appropriate present value. If such discussions are required, the employee and [non?] employee spouse should be required to contract privately with an actuary to determine that information. As you know, the Canadian Institute of Actuaries has provided guidance to its members on this process.

Our initial reactions are:

- There should be limits on the amount of information to be provided.
- The administrator
  - should be required to provide a present value amount which would be provided if the employee spouse had been terminated;
  - should not be required to provide any other present value amount, and

- should not as a general matter be involved in court proceedings. We are not sure that, in the nature of things, the administrator can be completely insulated: a court may well feel that in a dispute where the parties dispute the facts, the administrator is a necessary provider of information.

- If the information is limited to the kind of information provided upon termination of employment, we are doubtful about requiring payment of costs. Should the answer depend on whether it is customary for the plan administrator to charge a fee for a statement on termination? The circumstances seem analogous.

If more information is required, we are inclined to think that it should be for the parties to provide it, by whatever means they choose.

WE INVITE COMMENT.

H. Implementation

> ***Question 18: Where pension-division legislation should be placed.***
>
> ***Should pension-division legislation go***
>
> ***(a) in the Matrimonial Property Act?***
>
> ***(b) in a separate statute that applies to all pension statutes?***
>
> ***(c) in each pension statute?***

This is an important practical question. Should pension-division legislation be in a) the Matrimonial Property Act, b) in the Employment Pension Plans Act or in a special act dealing with division of pensions under all legislation, or c) in the specific pensions legislation? Since legislation is necessary, we think that this list exhausts the possibilities.

Putting pension-division legislation in each pension statute would make it easy for users to locate. We think, however, that it would have two disadvantages which would overbear that convenience:

- It would clutter the statute book with repetitions of the same provisions.

- It would create a serious risk that specific future amendments to specific pension statutes would result in different solutions to the same problem with respect to different pension plans. Ad hoc solutions to the same problems in different statutes would be likely to be ill-considered and would cause confusion.

If the orderly development of the law is the primary consideration, we think that the best place for division-of-pension legislation is in the Matrimonial Property Act. It is an aspect of the legislative scheme for the division of matrimonial property and can best be fitted into the overall scheme if it is in the statute that creates the scheme. It cuts across the various pension statutes and is best included in a general statute for the reasons given above. A countervailing argument might be that pension administrators would find it easier to deal with a provision in their own statute than with a provision in another statute, but it seems to us that additional inconvenience of noting a provision in the MPA would be minimal.

There is a further consideration. The federal Pension Benefit Standards Act, which applies to private-sector pension plans that fall under federal jurisdiction, provides that

> a pension benefit, pension credit or other benefit under a pension plan that is subject to provincial property law pursuant to this section is not subject to the provisions of this Act relating to the valuation or distribution of pension benefits, pension benefit credits or other benefits under a pension plan as the case may be.[48]

The PBSA defines "provincial property law" as follows:

> the law of a province relating to the distribution, pursuant to court order or agreement between the spouses, of the property of the spouses on divorce, annulment or separation.

It is highly likely that the Matrimonial Property Act falls within the definition of "provincial property law" and that a properly framed provision in it would therefore apply to pensions that fall under the federal PBSA. While it might be possible to frame a provision in the Employment Pension Plans Act that would fall within the definition of "provincial property law", and while it might be possible to frame such a provision broadly enough to cover pension benefits that are not within Alberta's legislative jurisdiction, such a provision would at best sit

[48] S. 25(4) of the PBSA, which gives a plan member power to assign all or part of their pension benefit to the non-member spouse on divorce, annulment or separation, overrides s. 25(3), so that such an assignment will be possible in any event.

awkwardly and at worst might be held to be pension legislation rather than property-distribution legislation.

We think that it is in the interests of spouses to have their affairs dealt with under one integrated legislative scheme for the division of matrimonial property. Therefore we think that the proposed Alberta pension-division legislation should be made applicable to PBSA pensions where the MPA applies to the division of spouses' matrimonial property. We think that, given the legislative situation described in the preceding paragraph, this is an additional reason for including the pension-division legislation in the Matrimonial Property Act rather than in pension legislation.

We think that the second-best place for division-of-pension legislation would be in either the EPPA or a separate statute that deals with division of pensions and nothing else. Putting it in one statute would be efficient in the sense that it would not repeat the same legislation in different pension statutes. It would also avoid the application of different solutions for the same problems. It might have a better chance of applying to federal PBSA pensions than would specific provisions in pension statutes. We therefore think that it would be better than having specific provisions in every pensions statute. It would not, we think, be as satisfactory as putting it into the Matrimonial Property Act.

We think it best that the Alberta pension-division legislation go into the Matrimonial Property Act and regulations under that Act. However, if insisting on an amendment to the Matrimonial Property Act will result in no legislation being passed, then the division-of-pension legislation should go into the EPPA or a separate statute that deals with division of pensions and nothing else. If insisting on that alternative will also stand in the way of reforming legislation, then identical provisions should be put into every pension statute. The main thing is to get division-of-pensions legislation. Where it goes is a matter of important detail, but it is not important enough to take the risk of getting no legislation at all.[49]

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[49] For a further discussion of this subject, see Pask & Hass, *Division of Pensions: the Impact of Family Law on Pensions and Pension Plan Administrators* (1993) 9 C.F.L.Q. 133, 150-51.

ALRI's Report 48 provided draft legislation. We do not think that at this stage there would be any useful purpose to be served by preparing another draft. When we see the results of consultation we will consider whether the preparation of a new draft based on our review would be useful at that stage.

WE INVITE COMMENT.

APPENDIX

RECOMMENDATIONS
Report 48, Institute of Law Research and Reform
June 1986

Recommendation 1
We recommend:
(1) that upon marriage breakdown the economic gain represented by the acquisition or an increase in value during marriage of a pension benefit should be divisible between the spouses under and in accordance with the principles of the Matrimonial Property Act and in particular the principle of just and equitable division.
(2) that in giving effect to those principles the following considerations should be borne in mind:
    (a) that it is desirable to avoid or to minimize future financial and business relationships between the spouses.
    (b) that it is desirable to facilitate and encourage settlements.
    (c) that it is desirable to minimize the financial and emotional costs of the division.
    (d) that income tax consequences of the division of matrimonial property should be taken into account, and that it is desirable to avoid attracting income tax which would not otherwise be payable.
(3) that the rights of third parties should not be prejudiced by the division of a pension benefit between the spouses.
(4) that the division of a pension benefit should not contravene the policy behind pension legislation.

Recommendation 2
We recommend that in dividing a pension benefit no account be taken of an actual or prospective change in an employee spouse's salary after the division unless at the time of the division the employee spouse has a right to receive the increase in salary or the employer has a right to reduce the salary.

Recommendation 3
We recommend that in dividing a pension benefit no account be taken of an actual or prospective improvement in the pension plan after the division unless at the time of the division the employee spouse has a right to have the improvement made.

Recommendation 4
We recommend that the legislation proposed in this report apply to a pension benefit under any of the following:
    (a) pension plans established by or under Alberta legislation, and in particular a pension plan established under The Alberta Government

Telephones Act, The Local Authorities Pension Plan Act, The Members of the Legislative Assembly Pension Plan Act, The Public Service Management Act, The Special Forces Pension Plan Act, The Teachers' Retirement Fund Act, and the Universities Academic Pension Plan Act.

(b) pension plans which are or ought to be registered under the Pension Benefits Act (Alberta).

(c) pension plans which are covered by reciprocal intergovernmental agreements under which the plans, insofar as they cover Alberta employees, are to be administered in accordance with Alberta law.

(d) pension plans which are established or registered by or under statutes which recognize Alberta law or Alberta court orders.

Recommendation 5

We recommend that, in order to give effect to the proposals made in this report,

(a) the Matrimonial Property Act be amended along the general lines indicated by the proposed legislation attached to this report, and

(b) that the amending legislation be given overriding effect with respect to pension legislation.

Recommendation 6

We recommend that the following methods of division of a pension benefit be used:

(1) a valuation and accounting, under which the employee spouse would retain the pension benefit and compensate the non-employee spouse for the appropriate share of the pension benefit.

(2) a valuation and division, under which the pension plan administrator would

  (a) pay for the benefit of the non-employee spouse the present value of the share in the pension benefit which the non-employee spouse is entitled to receive, and

  (b) reduce the employee spouse's pension benefit to reflect the payment.

(3) the provision of a separate pension for the non-employee spouse, under which the pension plan administrator would

  (a) pay to the non-employee spouse, on or after the earliest date at which the employee spouse could claim a pension and before the employee spouse's pension starts, a pension of a kind which is provided for under the pension plan which would have an actuarial value that is equal to non-employee spouse's share of the pension that the participant spouse could have claimed on that date, and

  (b) reduce the employee spouse's pension benefit to reflect the payment.

(4) a division of the proceeds of the pension benefit by the pension plan administrator.

(5) a division of the proceeds of the pension benefit by the employee spouse.

Recommendation 7

We recommend that the Court continue to have power to order a valuation and accounting.

Recommendation 8

We recommend

(a) that the Court be given power to order a valuation and division of an employee spouse's pension benefit under which the employee spouse has a vested right to a deferred pension,

(b) that upon a valuation and division the amount for the non-employee spouse's benefit be charged against the employee spouse's pension benefit,

(c) that upon a benefit becoming payable to the employee spouse under the pension plan the pension plan administrator upon the advice of an actuary shall make an appropriate adjustment to the amount paid out, and

(d) that regulations under the pension legislation provide for the making of the reduction in this way.

Recommendation 9

We recommend that the certificate of a pension plan administrator that a valuation and division of an employee spouse's pension benefit would prejudice the liquidity or the solvency of the pension fund be proof of the truth of its contents in the absence of evidence to the contrary and that it not be overridden unless the pension plan administrator has been given notice of an application for that purpose and has had an opportunity to give evidence and be heard.

Recommendation 10

We recommend:

(a) that the Court be given power to order the provision of a separate pension for the non-employee spouse where the employee spouse has a vested right to a deferred pension.

(b) that the separate pension shall start on or after the date upon which the employee spouse could claim a pension under the pension plan, but not later than the date upon which the employee spouse starts to receive a pension under the pension plan.

Recommendation 11

We recommend that where an employee spouse has a vested right to a pension which is locked in, whether or not payment of the pension has started, the Court

(a) be given power to order a pension plan administrator to pay to a non-employee spouse such portion of a payment of proceeds of the employee spouse's pension benefit as the Court may determine, and

(b) retain its existing power to order an employee spouse to pay to the non-employee spouse a share of the proceeds and to impose upon the employee spouse such trusts as are necessary to give effect to the order.

Recommendation 12

We recommend that upon a division of proceeds an employee spouse should make elections under the pension plan only with the agreement of the non-employee spouse or the approval of the Court, but that if the election relates to the employee spouse's employment, the Court should not withhold its approval unless it is satisfied that the election is not made in good faith.

Recommendation 13
We recommend that a death benefit payable under a pension plan be shared under a division of proceeds, except for any additional amount payable because the employee spouse is survived by a child or by a later spouse; but that a disability benefit not be shared.

Recommendation 14
We recommend that under the provision of a separate pension for the non-employee spouse, the Court be given power to order that a death benefit payable under the pension plan at any time before the separate pension is payable be shared, except for any additional amount payable because the employee spouse is survived by a child or by a later spouse; but that a disability benefit not be shared.

Recommendation 15
We recommend that a pension paid to a spouse as the survivor of an employee spouse be considered part of the pension benefit for the purpose of the division of proceeds.

Recommendation 16
We recommend that an order for the division of proceeds of a pension benefit shall not be affected by the death of the non-employee spouse and that the proceeds shall be payable to the estate or to the beneficiaries of the non-employee spouse.

Recommendation 17
We recommend:
(a) that the Court have power, in a matrimonial property order or at any time before an employee transfers a pension benefit from one pension plan to another, to direct that valuation and division be substituted for the provision of a separate pension or for the division of proceeds, and
(b) that the Court have power, in a matrimonial property order or at any time when any proceeds of a pension benefit have not been paid or remain in the hands of the employee spouse or his or her personal representatives and the payment of a separate pension has not started, to direct that division of proceeds be substituted for the provision of a separate pension.

Recommendation 18
We recommend that
(1) except as provided below, a pension benefit be divided before vesting and locking in by valuation and accounting.
(2) if a valuation and accounting would not be just and equitable because the vesting of the employee spouse's pension benefit is unduly delayed, the Court be given power to order that the pension benefit be divided by division of proceeds either by the pension plan administrator or by the employee spouse.

Recommendation 19
We recommend that if payments have started under a retirement annuity the pension benefit should be divided either by
(a) valuation and accounting, or
(b) division of proceeds either by the pension plan administrator or by the employee spouse.

Recommendation 20
We recommend
(a) that the proposed legislation establish an order of preference among the proposed methods of division,
(b) that the order or preference be as follows: 1) valuation and accounting, 2) valuation and division, 3) provision of a separate pension for the non-employee spouse, 4) division of proceeds by the pension plan administrator, and 5) division of proceeds by the employee spouse, and
(c) that a method of division later in the order of preference be adopted only if all methods earlier in the preference are inapplicable or beyond the Court's jurisdiction or would cause a result which would not be just and equitable; provided that the order of preference need not be followed if following it would cause hardship.

Recommendation 21
We recommend that, before vesting, a pension benefit, subject to any necessary adjustment for potential income tax liability, at the amount of any which the employee spouse would at the time of division of the matrimonial property be entitled to receive if his employment would be terminated at that time.

Recommendation 22
We recommend that under a defined contribution pension plan the value of an employee spouse's pension benefit be the amount of contributions and interest held for the employee spouse's account, including the vested portion of the employer's contributions and interest.

Recommendation 23
We recommend that under a defined benefit plan where the employee spouse has a vested right to a deferred pension the pension benefit be valued at the greater of
(a) the amount that the employee spouse would be entitled to if his participation in the pension plan had terminated immediately before the time of the valuation, and
(b) the present value of the normal pension which the pension plan would provide on the employee spouse's normal retirement date under the plan, or of the pension which an employee spouse has elected to take.

Recommendation 24
We recommend:
(1) that regulations be promulgated under the Pension Benefits Act or its successor Act and under the public sector pension statutes:

(a) adopting annually interest and discount rates to be used in valuing vested deferred annuities under defined benefit pension plans and providing tables of values for such deferred annuities.
(b) requiring a pension plan administrator, upon requisition by a spouse involved in negotiating or litigating the division of matrimonial property upon marriage breakdown, or upon an order of the Court, to provide in prescribed form the information necessary to determine the present value of the employee's normal retirement annuity.

(2) that the regulations be promulgated by the responsible Ministers after receiving the advice of an advisory committee which should include the officials charged with the administration of the pension legislation and persons expert in the disciplines involved in the valuation of deferred annuities.

Recommendation 25
We recommend that, if the law is changed to provide that upon termination of employment an employee is by law entitled to have an amount of money representing his pension benefit under a defined benefit pension plan transferred to another pension vehicle, an employee spouse's pension benefit shall be valued at that amount for the purposes of division upon marriage breakdown.

Recommendation 26
We recommend that if an employee spouse is already receiving a pension under a pension plan at the time of the division of matrimonial property, the pension benefit be the present value of the pension.

Recommendation 27
We recommend that a valuation made under Recommendation 23 and Recommendation 24 or under Recommendation 25 be binding for the purposes of a valuation and division.

Recommendation 28
We recommend that a valuation made under Recommendation 23 and Recommendation 24 or under Recommendation 25 or Recommendation 26 be binding for the purposes of a valuation and accounting.

Recommendation 29
We recommend that in determining the amount of a separate pension for a non-employee spouse a pension plan administrator value the pension which the employee spouse could claim and the pension to be provided for the non-employee spouse in the same manner as similar valuations would be made under the pension plan for the purposes of determining the amount of alternate optional forms of pension for employees and their spouses.

Recommendation 30
We recommend that the Matrimonial Property Act be amended to confirm that an employee spouse's pension benefit which began to accrue before the marriage can be pro-rated over the pre-marriage and marriage years.

Recommendation 31
We recommend that no allowance shall be made upon a valuation and division for the possibility that the employee spouse will not live until the commencement of a pension or for the possibility that one pension fund may not be sufficient to pay all pensions charged upon it.

Recommendation 32
We recommend that upon a valuation and accounting no allowance shall be made for the possibilities mentioned in Recommendation 31 unless a valuation without such an allowance would not be just and equitable.

Recommendation 33
We tentatively recommend that upon a valuation and accounting a deduction may be made for the potential effect of income tax, if any.

Recommendation 34
We recommend that the proposed legislation provide for the amendment of all pension plans to provide for the division of pension benefits in accordance with the Matrimonial Property Act.

Recommendation 35
We recommend that the government of Alberta pursue with the federal government discussions leading to the continuation of tax deferral for the proceeds of a valuation and division in the event that section 60(j) of the Income Tax Act is repealed or made inapplicable to them.