

Pension Benefits Overview

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As Canada's workforce ages, particularly with so many "baby boomers" nearing retirement age, interest is higher than ever in the subject of workers' pension rights.

Plan Types in Canada

Pensions are of two main types:

Defined Contribution ("DC") Pension Plans: in this sort of plan, regular contributions are typically made by the worker and the employer, often according to an agreed matching formula. Contributions are made to an investment account in which the employee normally can direct funds to the type of asset mix desired. Funds are locked in and not accessible until retirement at age 65. The amount of benefit that the employee will eventually receive depends on the particular investment experience - no payments are guaranteed.

Defined Benefit ("DB") Pension Plans: in this sort of plan, contributions may be made by both worker and employer, or employer only. The funds are often held in a pension trust fund, and the employee will receive a certain monthly pension payment after retirement. The amount of monthly benefit depends on the benefit formula contained in the pension plan text. Normally the formula will be based on the length of service and eligible earnings.

In Canada, both types of plans have advantages and disadvantages. DC plans offer the employee control over investment allocation, but with this comes a risk of loss from sub-optimum decisions. DB plans are more "conservative", in that the pension funds are normally managed by qualified investment advisors, and the benefit stream one can expect on retirement is more predictable - however there is less "upside" potential.

Vesting

This is a concept that may be important if Canadian employees quit or are terminated without many years of service with an employer. Pension plans in Canada normally provide that pension benefits "vest" after a certain number of years of continuous employment. If terminated after "vesting" occurs, departing Canadian employees would normally be entitled to receive either a lump sum (called the "commuted value") which would include their own contributions, with interest, but also the employer's contributions, or a deferred pension, the amount of which would be based on employer and employee contributions. If departure occurs before "vesting" normally the employee would only obtain his/her contributions back with interest. In all cases lump sums are only payable to a "locked in" investment vehicle.

Pension Plan Documents in Canada

Employees interested in understanding pension rights in Canada can request and review relevant plan documents. These would normally include a copy of the pension plan itself, perhaps the trust agreement under which pension funds are held,

plan booklets provided by the plan administrator, and individual pension plan statements that are normally circulated annually to plan members.

Pension Claims on Termination

Employees in Canada are entitled to actual working notice of dismissal. If employers choose to terminate without advance notice, they are in breach of contract, and must pay damages. In Canada, damages are normally assessed as the lump sum amount necessary to place the employee in the position he/she would have been in, if proper notice had been given. Damages include pension losses. The lump sum damage award should include an amount to compensate for the lost future pension benefits resulting from early termination. Often, an actuarial calculation is required to quantify this claim. Pension losses for the employee working in Canada may be quite significant, and should not be taken lightly. Particularly where individuals are dismissed near upcoming early retirement thresholds, actual damages can be much higher than the total of contributions that would have been made during the notice period.

Salary Continuation

In some situations, Canadian employees should consider the possibility of entering into a severance agreement based on continuation of salary and pension benefits. Particularly for older employees; those nearing retirement age, who do not plan to work again, salary continuation may suit the needs of both employer and employee. This can be particularly advantageous where the Canadian employee has a large vacation bank, and generous vacation entitlement, which may be used in some instances to enhance pension rights.

Surplus (and related) Claims

In Canada, in the case of Defined Benefit pension plans, surpluses may arise. Surpluses are monies held in the pension fund which are in excess of the expected future costs of defined benefits. Surpluses might arise because of unduly conservative actuarial assumptions which lead to overfunding, or from better than projected investment returns. Depending on the language of the pension plan that created the pension trust in the first place (subsequent amendments may not have been effective), surpluses may belong to employee/beneficiaries, or to employers. Canadian pension beneficiaries in DB plans may thus be able to receive a share in any existing surpluses, but not normally before the applicable plan is wound-up, in whole or in part. Surplus claims often include related claims of inappropriate use of trust funds to pay administrative expenses, and claims that the employers have taken improper "contribution holidays".

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