

Submission to the
Financial Sector Division
Department of Finance

Response to the Discussion Paper

“Strengthening the Legislative and
Regulatory Framework for
Private Pension Plans

Subject to the
Pension Benefits Standards Act, 1985”

Canadian Union of Public Employees

CUPE

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I. CUPE IS A MAJOR STAKEHOLDER

The Canadian Union of Public Employees (“CUPE”) would like to commend the Department of Finance for undertaking a public consultation on the *Pension Benefits Standards Act* (“PBSA”). The PBSA is very important to CUPE’s 570,000 members, thousands of whom work within federally-regulated workplaces in the airline, transportation, communications, and other industries.

As members of dozens of different pension plans in both the public and private sector, CUPE members have substantial first-hand experience and knowledge to contribute to the work of the Department of Finance, Financial Sector Division’s Consultation on pension policy reform (“the Consultation”).

The majority of our federal sector members belong to the defined benefit pension plans that the PBSA will cover, and we recognize that the changes proposed by the Department of Finance are likely to prove highly influential for other jurisdictions.

We would like to thank the Department for this opportunity to present the following written submission.

II. CONTEXT: THE PENSION SYSTEM IN CANADA

The third pillar of the system (occupational or private pension plans and private savings) is no longer meeting its objectives in “helping to bridge the gap between public pension benefits” and an adequate income in retirement for Canadians.

Only about a third of Canadians participate in a defined benefit occupational registered pension plan (“RPP”), the most secure form of occupational pension. More Canadians may accrue individual savings through Registered Retirement Savings Plans (“RRSP”) or other tax-favoured savings vehicles, but these vehicles leave participants exposed to significant risks.

The proportion of Canadians participating in RPPs has slowly and steadily declined for over 20 years, most particularly in the private sector. Despite regulatory and tax policy changes, and other significant changes in the Canadian economy, private occupational pension plans are not expanding their coverage, especially in the private sector.

This is a secular trend in the provision of occupational plans in Canada, and is also reflected in experience in jurisdictions with similar “three pillar” arrangements, such as the U.K. and U.S.

Given these trends in the coverage of private occupational pension plans, an important objective of a review of the pension system in Canada, particularly in the federal jurisdiction, should be consideration of alternative methods of securing adequate retirement income. Given the relatively limited effect of new policy measures in enhancing RPP coverage or retirement savings overall, major new policy options are appropriate to address adequate retirement income for Canadians.

The second overall challenge facing the pension system is the recent deflation in asset prices, particularly in equity markets.

While we acknowledge the significant difficulties facing all employers, a realistic assessment of the trends in pension plan coverage and pension plan funding are essential to developing

appropriate long-term policy responses. As a basic and fundamental proposition, the current economic conditions and financial difficulties facing sponsors are not **caused** by pension funding rules but instead by trends in labour markets and broader industry conditions, and in the past 18 months, a unique contraction in the equity and credit markets. While the long-term structural changes in the economy are relevant to long-term pension policy, short-term fluctuations (and once-in-a-century financial crises) are not.

Acknowledging the realistic causes of the current pressures will create a more appropriate and coherent public policy response.

These circumstances and causes suggest that the “appropriate means of enhancing the legislative and regulatory framework for registered pension plans” should have two primary objectives: addressing short-term liquidity problems of plan sponsors, and ensuring long-term security of benefits of employees and retirees.

What is not an effective or appropriate policy response to current conditions is to entrench long-term structural changes to temporary conditions, especially if such structural changes have the effect of transferring risk to those least able to control those risks, and least able to bear the costs of failure. Such a transfer of risk from sponsors to employees and retirees should not be a public policy objective.

Given these basic features of the pension system and trends within it, we believe the scope of the Consultation should be expanded or modified to consider both expansion of the first and second pillars of the system. However, we do not think that merely expanding the first and second tiers are sufficient policy responses. RPPs are and will remain an important component of retirement income of Canadians. To this end, we believe that a priority in any policy response to the challenges to retirement savings must include initiatives to expand defined benefit RPPs. Our submissions will identify the limits of a “supplementary” or expanded tier two program, and emphasize the role of occupational defined benefit plans.

III. MANDATE OF THE CONSULTATION

Focus on the Right Factors

We have noted that the most recent research shows that the factors driving pension coverage in Canada are labour market changes. This research has also shown that the two primary factors associated with the presence of a defined benefit plan (or any RPP, for that matter) are (i) the presence of a union and (ii) the size of a firm. The main factors supporting occupational pension plans in Canada are large, unionized employers. If the RPP system is to be enhanced in Canada, it will be done through supporting and expanding unionization of workplaces, and, where possible, consolidating employee participation into larger pension plans.

The scope of the Discussion Paper does not take these factors into account. As a result, the Discussion Paper and the Consultation do not focus on some relevant and significant policy questions. The two most fundamental oversights are the importance of strengthening Tier I and Tier II programs as sources of retirement income, and the crucial importance of promoting defined benefit pension plans as the optimal structure for providing private retirement income.

Expanding Tier I and Tier II

Tier I and II programs are designed to ensure a minimum retirement income through the use of mandatory enrolment, indexation, portability and disability provisions. These programs, particularly Tier I programs Old Age Security and Guaranteed Income Supplement, should be reviewed with the objective of expanding their coverage, which would have the maximum impact on all Canadians.

Another long-standing proposal of the union movement generally is to expand the Canada and Quebec Pension Plans ("C/QPP"), through an increase in benefits and an increase in contribution levels of the **existing CPP benefit structure**.

The effect of expanding C/QPP would be immediate, structural and effective to meet the requirements of:

- providing some limited relief to sponsors of occupational plans (in particular through existing off-set mechanisms built into some occupational pension plans),
- expanding coverage of pensions to Canadians, and
- enhancing secure benefits to all.

CUPE strongly urges the Department to consider the expansion of the existing CPP plan benefit and contribution levels, and to consult with provincial governments about this initiative.

At the same time, CUPE does not support the creation of a “supplementary” Tier II plan that does not provide defined benefits. CUPE is familiar with Keith Ambachtsheer’s recent proposal for a supplementary tier or level of the CPP designed as a defined contribution plan. While we strongly support expanding pension coverage in a large, government-backed pension savings vehicle, *the optimal plan design from a public policy perspective is a defined benefit plan*. There is evidence in the U.S. and Canada (including studies by Ambachtsheer himself) that defined benefit plans are excellent value propositions for delivering stable, secure and affordable retirement incomes.

Very simply, large defined benefit plans are **the optimal vehicle** for leveraging size and absorbing and re-distributing investment and discount rate risk. Defined contribution plan designs can leverage lower unit costs, but ultimately leave individual plan participants to face significant investment and discount rate risk. Recent studies in the U.S. show that these risks can alter retirement incomes by as much as 30% compared to defined benefit plan designs, even with low unit costs.

Finally, the expansion and enhancement of the current Tier I and Tier II programs **should not be considered a replacement** for enhancing defined benefit RPPs. Private, occupational pension plans provide up to half the total retirement income for most low and middle-income Canadians. RPPs are playing an important and increasingly important role in providing retirement income. As such, these plans, most particularly defined benefit plans, must be a priority for policy reform.

Defined Benefit Plans are a Priority

Within the scope of the current review, CUPE views defined benefits as the best form of benefit available to employees and retirees. CUPE and employees across Canada have long bargained to establish and maintain defined benefit pension plans.

Defined benefit plans are superior pension plans in most respects. These plans are a secure form of pension promise for members and retirees, and provide a level of certainty and security that permits both career planning and retirement with dignity. Defined benefit plans are also the most cost-efficient form of saving for retirement, that benefit from pooling investments to create leverage and lower unit costs, and spreading the impact of adverse experience.

The Discussion Paper also notes a shift from defined benefit plans to defined contribution plans. While there is evidence of a shift in plan design, including conversion from defined

benefit to defined contribution, the vast majority of members still belong to a defined benefit plan. Research has shown that defined benefit plans (or plans similar in design, such as multi-employer plans), are the dominant plan design. We estimate that more than three-quarters of all plan members in Canada belong to defined benefit plans. Defined benefit plans should be contrasted to defined contribution plans, which are much riskier to members. Defined contribution plans expose individuals to significant investment and interest rate risk, and make it harder to plan both careers and retirement. Defined contribution plans are on the whole worse value propositions for members, carrying higher unit cost fees and fewer protections for members and retirees. The impact of recent experience in the market has demonstrated the very significant risks borne by members of defined contribution plans. Defined contribution plans are not able to deliver the retirement savings that members and retirees deserve.

In short, we believe that defined benefit plans are the most appropriate distribution of risks between employers and employees and retirees; defined benefit plans make an appropriate distribution of risks on the parties most able to bear them, except in extreme circumstances, such as insolvencies.

Consequently, we believe that regulatory and legislative reform should prioritize the protection and encouragement of defined benefit plans in Canada.

IV. PRINCIPLES GUIDING POLICY REFORM

Notwithstanding the fundamental causes behind the decline in coverage of RPPs, we note that in the absence of more significant reforms, the occupational pension system provides an important – and increasingly important – contribution to retirement incomes of most Canadians.

In the regulation and oversight of this private system of pension provision, the Discussion Paper states guiding principles of the Consultation, namely:

- The voluntary nature of private or occupational pension provision, which is supplemented and expanded by fiduciary duties and other statutory provisions normally applicable when the property of one person is administered by another;
- The asymmetry of information about and control over most pension plans, a common asymmetry in the employment relationship, which requires heightened disclosure about pension plans to their beneficiaries; and
- The pivotal role of regulatory minimum standards in ensuring pension plans are administered in the best interests of their members and retirees and meet the pension promise.

We observe that at least one of these principles, while historically relevant, is now seriously challenged as an appropriate principle of public policy. The proportion of the labour force participating in occupational pension plans has decreased slowly and steadily from a peak in the mid-1970s to about a third of the paid Canadian labour force today. In short, the voluntary occupational pension system is not delivering the goods. Occupational pension plans exist almost exclusively in workplaces where there is a collective bargaining agent.

Unions have long fought and bargained to establish and maintain pension plans. We therefore question the priority of the “voluntary” system of occupational pensions in public policy, when they are not available to the majority of the paid labour force, and when they are usually co-incident with unions fighting to establish them.

We also do not believe that the Discussion Paper fully articulates the principles behind pension policy in Canada. It tells only half the story of pension policy in Canada. Pension policy and regulation has and will continue to incorporate the following principles:

- The adequacy of retirement income from public and private pension sources, ensuring the dignity of Canadians in retirement;
- Expanding coverage, thus ensuring fairness and equity in the provision of opportunities to save for retirement, whether through private or public vehicles; and
- The security and stability of the pension promise, in both the private and public pension context.

Together, we believe that these six principles should inform the scope and balance of the recommendations of the Department.

V. SPECIFIC ISSUES FOR DEFINED BENEFIT PLANS

Entitlement to Surplus

The Discussion Paper also articulates the long-standing debate over entitlement to surplus.

CUPE views pension funds as holding workers’ deferred wages. In practice, we know very well that all pension contributions made by employers are incorporated into their calculation of their payroll cost, and this cost directly informs their bargaining (both formal and informal) around wages and other compensation.

These deferred wages are earned at the time that contributions are made – not at the time that pension benefits are eventually paid out. When contribution requirements rise, and when deficiency payments are required of employers, these cost increases automatically and understandably affect the employer’s negotiating position on other cost and compensation issues.

In this light, the claim that employers suffer from an “asymmetry” of risk and reward with defined benefit pension plans is entirely spurious. The risk faced by employers who face short-term pension liability is ultimately, always, shared with their workers. The overarching risks faced by workers – of pension benefit cuts, of contribution rate increases, of plan “conversions” – tend to go unmeasured in these equations.

Our position on this debate is that assets of pension funds, and income on them, should be used for the purpose of the pension plan: the benefits of members, retirees and their beneficiaries. We view pension plans and funds as pools of deferred wages in the custody of an administrator.

We acknowledge that as a basic rule, the plan documents have given expression to this entitlement. With respect to a limited group of plans whose entitlement is at best ambiguous, over the past 20 years, a significant body of case law has examined this issue in very great

detail, and with a large expenditure of resources, and created a balance between these two positions on entitlement. We submit that the balance struck by this case law is appropriate, and public policy should reflect it.

However, where regulation intervenes in these private arrangements, as a matter of principle, that regulation should ensure that surplus arising from pension fund assets remains the property of the pension fund, and ought to be maintained in the pension plan for the benefit of plan members and retirees. It should not be diverted to other uses.

We also note that the argument that “asymmetry” in pension surplus entitlement **is not a major factor** driving pension coverage, and should not be a major factor driving pension funding decisions. The most recent and comprehensive research available demonstrates that pension coverage is driven primarily by long-term structural changes in labour markets, and not by “asymmetry” in surplus entitlement.

Second, pension funding ought not to be subject to standards that permit systemic under-funding. Pension funding must meet the minimum standards established by regulation: that is one of the primary and fundamental purposes of the regulation of occupational pensions. To the extent that those standards permit systemic under-funding, they should be strengthened to require full funding over the long term. Plan sponsors should not have the option or the choice to systemically under-fund pension plans over the long term, or “minimally fund” pension plans. If sponsors deliberately under-fund pension plans, this indicates that regulatory minimum standards should be strengthened.

Third, it is not true that sponsors bear all the “downside risk”. We submit that pension plan members bear some of that risk through contribution increases or wage concessions, and more importantly, always ultimately bear the risk of a sponsor becoming insolvent when a plan is underfunded. In current economic conditions, this is a serious and significant risk to plan members. Any assessment of the “asymmetry” argument must acknowledge the serious risk of sponsor failure borne by plan members and retirees.

We submit that more appropriate policy responses to short-term challenges facing plan sponsors, most notably deflation in asset values leading to higher contributions (at least temporarily), is to provide forms of relief specifically targeted at those issues.

Contribution Holidays

Pension plans and funds should not be a profit centre for sponsors, and pension policy should not enable them to be one.

At a very general level, pension funds enjoyed very significant surpluses through the 1980s and 1990s. Tax policy had the effect of creating contribution holidays during this period – all too often without reporting this to plan members. When asset values dropped in 2000-2002 and again in 2008, sponsors were forced to start making their full current service contributions again and in many cases to add additional payments to amortize deficiencies.

CUPE urges the Department to examine the recent spate of deficiencies closely. A research analysis published in June 2005 reviewed the data on employer contribution holidays in the British Columbia and federal jurisdictions. They discovered that these holidays – resulting in huge cost savings for sponsors - were a significant factor in the emergence of the later deficiencies.

Of the 42 significantly under-funded (i.e. going-concern funded ratio of 80 to 89.9 per cent) or extremely under-funded (i.e. going-concern funded ratio of 70 to 79.9 per cent) pension plans in the study, *45 per cent would have completely eliminated their current actuarial deficit if contribution holidays had not been taken.*¹

This study also showed that in many cases, the employer involved recognized the funding deficiencies, but they continued to take them (and put funding security at risk).

OSFI documents show that that in 2003/2004, 16 federally regulated pension plans continued to take contribution holidays when they were aware that they might no longer be in a surplus position...While these plans resumed their contributions following OSFI's enquiries, the regulator's findings raise concerns about employers' contributions, as well as policy and enforcement practices related to contribution holidays.²

There are two specific cases in the federal jurisdiction that highlight the danger of contribution holidays: Canada Post and Air Canada. In both cases, contribution holidays have been taken inappropriately while the plan's funded position deteriorated. If contributions holidays had not been taken by both these plans, the impact of the current market experience on the businesses and balance sheets of both employers would be significantly reduced, and they would be much better positioned to meet new challenges.

¹ SHARE, "Taking a Holiday: The Impact of Employer Contribution Holidays on the Funding of Defined Benefit Pension Plans," Research Report, June 2005, p. 5-6. Available at: <http://www.share.ca/files/Taking%20a%20Holiday.pdf>

² Ibid. p. 11.

Tax Policy and Excess Surplus

CUPE has long supported the federal government reviewing the current threshold applying to excess surplus in defined benefit RPPs. We support raising this threshold to a higher amount than 110% of liabilities.

The ITA requirement of employer contribution holidays in instances where valuations show an “excess” surplus has only exacerbated the current under-funding problems by cutting off the employers’ ability to pre-fund plans. CUPE has repeatedly argued, along with many in the labour movement, that the excess surplus rules in place and the “remedy” of employer contribution holidays were ill conceived at the outset and should be repealed.

We note that on this issue, our critical view is shared by analysts at both the C.D. Howe Institute and the Certified General Accountants Association of Canada. Both groups have argued that the existing excess surplus thresholds are too low and should be immediately raised.³ Our view is that the original “excess” threshold was never justified, and that even if it were, benefit security or enhancement ought to have been the priority for eliminating such “excesses”. Plan members should benefit from positive plan experience.

Solvency Funding Rules

We submit that defined benefit plans should be subject to solvency funding rules. Solvency funding rules are intended to provide a form of benefit security in the event of a plan wind-up or sponsor insolvency, in short, to ensure the pension promise in the event of adverse conditions.

As suggested by our analysis in the previous section, we do not believe that the solvency rules, *per se*, are a fundamental cause of pension under-funding and consequent pressures on contribution rates. Solvency funding rules merely reflect current economic conditions. Solvency rules should be fit for their purpose – to measure the solvency position of a plan, on a realistic, market-based basis, at a given point in time. Deviations from this principle do not meet the purpose of solvency measurements, and erode the security of the plan.

The Discussion Paper raises the possibility that the temporary extension of solvency amortization periods from five to 10 years be made permanent. We strongly oppose this proposal. Extending the payment period of solvency deficits defeats the purpose of solvency funding, which is to ensure fully funded benefits in the event of plan termination in an underfunded position, and typically, an insolvent sponsor. In the absence of other robust protection of benefits, solvency funding is the primary mechanism by which benefits are secured for members and retirees. Extending amortization periods effectively shifts the risk of under-funding to members and retirees, including the risk associated with the insolvency of the sponsor. We believe that this shifts risks on to those least able to control those risks, or to cope with the event of failure.

Temporary Solvency Relief

While we have serious concerns about the erosion of benefit security implied by the temporary solvency relief measures announced by the Government, CUPE believes they

³ See Laidler and Robson, *Ibid.*, p. 9 and CGA-Canada, *Ibid.*, p. 44.

deserve serious consideration when balanced by adequate protections for benefit security. The terms of the temporary solvency relief create a balance of interests that address one of the key effects of the deflation in asset values in 2008.

The fundamental relief provided is the ability to reduce payments to a pension plan in respect of solvency deficiencies, and make those payments over a longer period of time. This relief amounts to the extension of credit from pension plan members and retirees to pension plan sponsors. In order to provide adequate protection for this extended credit, the federal government has proposed several protections, including:

- The requirement for member consent to changes to amortization schedules;
- Securing the difference between five and 10 year amortization schedules through letters of credit;
- Creating a special pension charge under the *Bankruptcy and Insolvency Act* (Canada) that would “secure” the difference between five and 10 year solvency funding in the event of a liquidation; and
- Not extending relief to existing solvency deficiencies amortized over 10 years (under terms of prior relief provided to sponsors).

We endorse proposals that are balanced, temporary, transparent, fair and coherent public policy response to current conditions.

We strongly oppose making 10-year amortization a permanent change to solvency funding rules, and we further strongly oppose extending this relief without the conditions contained in the Government proposal.

Experience in Ontario with the “too big to fail” regulation to the Ontario *Pension Benefits Act* is relevant to consider against proposals to permanently extend credit (through solvency relief and related measures) to pension plan sponsors on a long-term basis. Exempting certain very large plans from some funding rules during the recession of the early 1990s is now widely recognized as being a fundamental cause of under-funding today. This under-funding has and will cause very significant government expenditures of the participating sponsors in that regulatory relief, and did not result in the policy objective of improving plan funding over the long term.

Temporary solvency relief described above has the effect of providing short-term liquidity to targeted sponsors, in order that they meet their funding obligations. This is not a long-term fix to the problems of declining coverage (as a proportion of the paid labour force) in occupational pension plans, nor is it a solution to the long-term under-funding of pension plans.

Letters of Credit

As an alternative or complement to short-term solvency relief, one of the most direct ways to address short-term funding volatility in the current climate is to create a facility for government to directly extend credit to sponsors for the purpose of meeting pension funding requirements, and who demonstrate need. Such credit could be extended on a temporary and secured basis. This form of relief would be targeted, controlled and strike the appropriate balance between benefit security and short-term liquidity needs of sponsors.

The Discussion Paper also suggests that the amortization period for solvency deficits be (i) linked to the financial health of the sponsor and (ii) kept the same, but funded through letters of credit purchased by the sponsor but in favour of the plan.

In general, we support empowering the regulator to monitor the financial health of plan sponsors, and to require the filing of financial information to facilitate this monitoring. We believe that in order to effectively be pro-active in administering the PBSA, the regulator must have adequate resources and information to prevent serious under-funding of pension plans.

We do not support, however, extending amortization periods based on the financial health of the plan sponsor. Extending amortization periods to “unhealthy” sponsors places very significant risks on plan members and retirees at precisely the time they are least able to bear those risks. (Conversely, extending amortization periods to “healthy” sponsors provides relief to those who do not need it.)

The implementation of such relief may also be difficult for the regulator, with its current powers, to administer. The regulator would have to review and judge sponsors’ credit-worthiness (or other measures of “health”), a judgment that may have wider impacts for plan sponsors.

CUPE acknowledges that letters of credit have been permitted or recommended in several provincial jurisdictions. However, we do not believe that funding pension plans through letters of credit will address problems of under-funded plans. In general, sponsors who are facing cash flow problems will not be able to secure letters of credit at reasonable prices. Sponsors who may obtain such credit will generally already be credit-worthy and able to commit cash resources to a pension plan.

We believe that, if adopted, the use of letters of credit should be strictly controlled. Limits should be placed on the percentage of solvency deficits that may be secured through letters of credit, letters of credit should be irrevocable and clearly assets of the plan, and their use should be time-limited, reflecting the temporary nature of short-term cash flow problems.

Full Funding on Plan Termination

CUPE supports the introduction of a statutory requirement to fully fund defined benefit plans upon termination of the pension plan in accordance with the conditions stated in the Discussion Paper, namely, payments made according to the most recent valuations and no more than five years after the date of plan termination.

It is CUPE’s position that the very nature of pension arrangements, contracts supplemented by fiduciary duties, would otherwise require the full payment of unfunded liabilities upon plan termination in any case. To permit the termination of unfunded plans is to fundamentally alter the pension promise.

We support the codification of this requirement, and note that most Canadian jurisdictions already require this as a minimum standard.

However, we believe that all unfunded liabilities of pension plans should be placed in priority in the event of a bankruptcy, and not rank equally to other unsecured debts of the bankrupt. CUPE submits that pension liabilities should have the same priority currently accorded other pension liabilities, namely current service costs, in the *Bankruptcy and Insolvency Act* (Canada).

National Pension Insurance

Many of the proposals in the Discussion Paper, and several proposed by stakeholders, have the basic effect of extending unsecured credit to plan sponsors. This is achieved through longer debt repayments schedules, lowering contributions to pension plans, or changes to technical standards that apply through pension regulation. This extension of credit – at a time

when credit is unavailable from private sector lenders – is a significant transfer of risk and financial resources, from plan sponsors to employees and retirees.

If these proposals are adopted, then the Government reforms will transfer significant risk from those more able to control it to those much less able to control it. We do not believe that this is an appropriate public policy.

Therefore, a second fundamental initiative that can address the short and medium term pension policy objectives is the establishment of a self-funded but government-backed and administered federal occupational pension insurance scheme.

In the absence of strong solvency funding rules, such an insurance system would provide a level of protection for employees and retirees whose plans are under-funded and whose sponsors fail.

Other jurisdictions have similar schemes, including Ontario, the U.S. and the U.K. Such a scheme would ensure that, if and when solvency relief is extended to sponsors and plans, and sponsors nonetheless fail, pensions of retirees and members can be secured, at least in part.

Investment Rules

A very specific investment issue that is central to CUPE's submissions is the impact of privatization on defined benefit plans. As a trade union representing over 570,000 of the workers in Canada that are most directly targeted by privatization and contracting-out, we are very well positioned to provide answers to this question.

In most instances, the central driving force behind the recent moves to privatize public services, public infrastructure and public sector employment, has been the desire to cut government costs. Of course, such cost cutting translates into real, material effects on the workers involved: alongside de-unionization, wage losses, and employment insecurity, privatization often results in workers losing their pension plan.

One of the especially problematic developments in recent years in the evolution of pension fund investment has been the increasing role played by large pension funds in financing the very privatizations discussed above. Large pension funds have been increasingly sought out as underwriters and financiers for major privatization projects. As the C.D. Howe Institute recently reported enthusiastically:

Private-sector and government-worker plans are scouting the world for investments in power and gas transmission, water, roads, bridges and tunnels, airports and ports...More Canadian savers, large and small, would do well to get a piece of this action.⁴

Notwithstanding the implication of this commentary, the novelty of this development is not the fact of pension fund investment in infrastructure. Pension funds have long been relied upon to invest in the government bonds issued for financing capital-intensive infrastructure projects. Indeed, the original reserve fund of the Canada Pension Plan was dedicated almost exclusively to funding this valuable infrastructure via purchase of long-term bonds

⁴ William B. P. Robson, "Found Money: Matching Canadians' Saving with their Infrastructure Needs," C.D. Howe e-brief, March 8, 2007. Also see John Chenery, "Financing the Future: Building Canadian Infrastructure," *Summit Magazine*, Focus Issue: Public-Private Partnerships, 2001.

from the provinces. The innovation that attracts the C.D. Howe's Institute's interest is that the pension funds described are taking over direct ownership and control of these assets, and operating them as private, for-profit investors. In several cases, pension plans have become direct and indirect agents of privatization – a development that the Institute ideologically supports.

CUPE and many other trade unions have argued strenuously that P3s are bad public policy. We have shown that it always costs the government less to borrow than it would cost a private corporation. P3s arrange for a government to pay a private corporation to go out and borrow on the government's behalf, at a cost of borrowing that is substantially higher than the government's own direct borrowing cost.

The result, consistently, is that P3 projects generate much higher costs (for the public “partner”) than if the same project were pursued on a traditional public sector model. This conclusion is being reached by an increasing number of independent research studies, including one released just weeks ago by the Federation of Canadian Municipalities. Their analysis, focused on municipal sector P3s, concluded as follows:

To make infrastructure investments, municipal governments can easily borrow almost all the funds they need at very favourable rates. Indeed this fact is so clear, it is rarely challenged. To leave the responsibility of financing to the private partner is a poor solution to a non-existent problem, when traditional municipal financing is simple, relatively easy and, above all, **much less costly than the private-sector equivalent**. Nevertheless, the truth is that some people have an interest in making us think that there is a problem ... because they have solutions to sell.⁵

We outline this argumentation and research at such length for an important reason. We consider our policy critique and our opposition to these projects to be based on fundamental principle. Our position has also been repeatedly ratified by our membership. In addition, our National structure voted to approve a policy statement in 1999 that called on the trustees and managers of CUPE member pension plans to resist the promised returns associated with these projects and turn them down on the ground that they are not in the interest of plan members, nor of taxpayers.

Yet, many of our own pension funds are still being used against us. Even in cases where CUPE is able to name one or more trustees to a decision-making Board that sets out investment policy, they are often advised that their fiduciary obligation to plan members *requires* them to invest in P3s – even where it can be shown to be bad public policy, bad for public services, and bad for workers’ pension coverage. The argument advanced, stripped down to its most simplistic formulation, is that fund trustees are obliged to aim to “maximize” their rate of return, and rest indifferent to all “non-financial” considerations.

While CUPE takes issue with this simplistic formulation of the legal parameters of fiduciary duty, there is no doubt that ambiguity and dispute over this issue remains. Just as with an older (but continuing) debate about “socially responsible investment” (“SRI”), our struggle to restrain aggressive and (in our view) high-risk privatization investments is hampered by the lack of clear language in the PBSA that would expressly permit and legitimize such considerations or exclusions. While CUPE certainly recognizes the need to earn “reasonable” returns on fund investments, we reject the notion that this responsibility creates an absolute obligation to support every high-yielding project developed.

CUPE’s concerns regarding pension investment trends extend beyond just P3s and privatization. We are also seeing rapid growth in more complex and less transparent financial vehicles and instruments that are being increasingly marketed to pension funds. Hedge funds, private equity funds, highly leveraged and “short-sell” investments, and various types of derivatives are becoming more popular as pension fund investments.

⁵ Pierre J. Hamel, “Public-Private Partnerships (P3s) and Municipalities: Beyond Principles, a Brief Overview of Practices,” Institut national de la recherche scientifique, Commissioned by the Federation of Canadian Municipalities, August 31, 2007. Emphasis added. <http://www.fcm.ca/english/media/backgrounders/p3report.pdf>

As the “asset-backed commercial paper” (“ABCP”) crisis illustrates, pension funds are increasingly becoming involved – perhaps even lured – into complicated investments whose risk profile may be beyond their current capacity to measure and monitor.⁶

⁶ We would argue that all boards and Administrators – including so-called “lay” boards and “expert” boards – face the capacity problem identified here.

For example, in the course of his reflections on the 2006 fiasco surrounding a collapsed U.S.-based hedge fund called Amaranth, one hedge fund manager admitted:

Hedge-fund strategies have become so obtuse, their sales pitches so aggressive, and their monitoring so lax that one could question whether anyone should be in these funds, let alone pension-plan managers who have no ability to judge what these funds are doing and are supposed to invest regular folks' money in relatively safe places.⁷

A related but separate set of concerns is also emerging in relation to the rapid recent growth in private equity as an asset class for pension funds and other financial investors. A February 2007 submission by a Europe-based international hotel and food workers' union to British Members of Parliament sounded a serious alarm about the increasing domination of financial markets by private equity. The union describes private equity funds as follows:

Enormous pools of money provided largely by institutional investors and managed by the fund for the purpose of acquiring other companies in whole or in part, delisting them from stock exchanges if they are publicly listed, restructuring them and then selling them to other investors, either through public stock offerings or to another buyout fund. While private equity firms have traditionally set targeted rates of return of 20 to 25% annually, the largest funds have generated returns of 40% a year over the past 10 years.⁸

The union presents disturbing evidence of a virtual explosion of private equity buyouts and sell-offs, and argued that the scale of these deals – particularly their highly leveraged character – poses risks to the financial system as a whole. Moreover, they suggest that the funds (with the associated leverage) are so large that all public corporations have become potential takeover targets (an observation familiar to many observers of recent shifts in Canadian financial circles). The effect, they suggest, imposes a serious cost on workers affected:

A pre-bid environment hangs over the economy as a whole, meaning short termism is institutionalized, bringing with it more job cuts and more attacks on wages and working conditions and more attacks on trade union rights.⁹

While it is possible that Canadian practices with private equity are more benign than this, CUPE

is nonetheless concerned about these dynamics and their implications for our members (and their pension coverage). While promising – and perhaps delivering – substantial rates of return to pension fund investors, such predatory investment practices are anathema to the trade union movement and to CUPE members. We certainly do not expect that our pension funds will be secured - or workers' defined benefit pension coverage improved – through such practices.

Rather, as negotiators of pensions, and as a trade union that names pension fund trustees to various Boards, CUPE is concerned that pension fund trustees and money managers face legal arguments about the need to “maximize” their rate of returns within a new and rapidly changing environment. We are concerned that aggressive marketing campaigns by financial specialists and marketers may be pressuring pension fund trustees and money

⁷ James J. Cramer, “After Amaranth,” *New York Magazine*, September 22, 2006.

⁸ Peter Rossman, “Presentation to Trade Union Sponsored Labour MPs on Private Equity and Leveraged Buyouts,” International Union of Food, Agricultural, Hotel, Restaurant, Catering and Allied Workers Associations (IUF), February 27, 2007

⁹ *Ibid.*, p. 5

managers to pursue strategies that are both riskier and more punishing to affected workers than their advocates are inclined to admit.

Raising Minimum Standards

As with real funding security, the minimum standards established in the existing system represent important and hard won gains. Defined benefit pension coverage would not be as high as it is today were it not for the existing rules on vesting, eligibility, and portability.

We would suggest, however, that there is still significant room for improvement to the minimum standards. CUPE represents many of the growing number of precariously employed workers – part-time, temporary, and contract workers who struggle from job to job, either excluded from participation in workplace pension plans or unable to vest, defer or transfer entitlements when they do earn them.

Moreover, we are very aware that it is workers that face discrimination and disadvantage in the labour market – women, new Canadians, people of colour, workers with disabilities, etc. – that are disproportionately represented in these categories. Under the existing rules, even part-time workers who become permanent and long-term will self-exclude by opting-out. As a result, these same workers are far less likely to build up decent pension entitlements by the time they are ready to retire.

Immediate and valuable extension of defined benefit pension coverage could result from relatively simple and low-cost improvements to the standards in place. The province of Québec has shown that immediate vesting is viable. Coverage could also be extended if rules were established requiring that part-time workers be required to join pension plans anywhere that full-time workers' participation is mandatory.

Partial Wind Ups

The PBSA contains some minimum standards in the event of a partial or full wind up of a pension plan. We note that these currently include a requirement to immediately pay all current service costs, special payments and employer and employee deductions. The PBSA also provides that members affected by a partial wind up have the same rights and entitlements as they would have on a full wind up.

The Discussion Paper asks whether provisions dealing with terminations in partial wind ups be eliminated from the PBSA altogether. CUPE's view is that these are the very minimum standards that must apply to RPPs, and that in fact, the PBSA is both vague and incomplete in its treatment of full and partial wind ups.

In the case of both full and partial wind ups, we believe that the regulator should be provided with greater powers to require both terminations and full or partial wind ups including the distribution of assets to members affected by a wind up. The current PBSA permits the regulator to order "terminations", but only provides a discretionary power to complete the wind up.

More importantly, in our view, the lack of more meaningful protections of members and more portability of defined benefit pension entitlements is a serious weakness of the existing system. The result is that many workers are forced to choose between deferring an entitlement (which often means sacrificing the wage-indexation that would otherwise have applied to it), and transferring the value out to a locked-in RRSP and seeing the benefit promise erased.

Earned pension entitlements should be more secure than this, and the idea of portability should be facilitated. For example, the PBSA should strengthen the obligation on employers to accept transfers-in of accrued locked-in pension entitlements from either individuals or transferring-in groups of workers. The fact is that employers and administrators consider such transfers to be an administrative irritant and cost that they increasingly choose to avoid. While this may be understandable, such transfers are key tools for preserving and building secure defined benefit pension entitlements. Workers' confidence in the defined benefit pension system would be greatly enhanced through such positive innovation.

Second, long service plan members who are terminated individually or in groups as part of a restructuring do not have adequate protection of their defined benefits. Due to the nature of defined benefits, their value grows significantly in the final years approaching retirement. Members who are terminated prior to reaching retirement age may be unfairly denied early retirement benefits or other ancillary or bridging benefits. Most recently, the Ontario Expert Commission on Pensions examined the issues involved in partial wind ups, group and individual terminations and recommended extending "grow in" benefits to all terminated members of a pension plan. We support this recommendation.

Phased Retirement

The minimum standards of the PBSA and regulations that we aim to defend and improve are complemented by important and related standards established by the ITA. One of the federal tax rules on pensions that has recently been subject to review and amendment is the restriction on continuing to work with an employer whose pension plan is paying out a pension benefit. This framework – sometimes considered a version of "no double dipping" – established the concept that pensions are for retirement, and they are tax-assisted because there is a public interest in ensuring that more workers are able to retire with income security.

The federal budget of March amended the ITA to change this framework – possibly quite dramatically. Under the rubric of "phased retirement", the proposal contemplates a liberalized system where employers will be permitted to begin pension payments to eligible (i.e. older and long-service) workers that remain in the workforce. While phased retirement is usually described as a system to replace sudden retirement with a more gradual withdrawal from the workforce, the budget proposal would actually permit employers to begin paying pensions to workers that continue to be employed full time.

Although we recognize these changes have been made, CUPE continues to have serious reservations about this direction for pension policy, and suggests that they be revised. We can imagine such models of phased retirement being applied in ways that undermine trade union wage bargaining and envision the use of pension funds to supplement and subsidize employers' payroll. Further, this model is being proposed alongside three other retirement age related developments:

- Legal norms regarding the age of "mandatory" retirement are changing in many provinces;
- Many employers are concerned about a rapid exit of experienced workers from the workplace in the coming 10-15 years;
- More and more employers and industry organizations favour an increase to their plan's age of eligibility for retirement and a discontinuation of programs for early retirement as a means to reduce pension liabilities.

In this context, the proposal to permit pension funds to begin flowing to workers who continue working – potentially indefinitely – is disturbing. We can envision a situation where a growing percentage of a given workforce is receiving “extra-pay” (i.e. regular wage plus pension), possibly to a level that is the same or more than their regular pay, for the same or less hours of work.

CUPE is concerned that the effect of such an arrangement will be to introduce a second, advantaged category of worker into the workplace and thereby undermine collective bargaining and trade union solidarity. Finally, we foresee such models strengthening the campaign already under way to raise the “normal” age of retirement for both workplace and public pension plans from the current standard of age 65 to 67, 70, or beyond.

Mandatory Indexation

CUPE has always supported the principle that workers' pensions should not have their purchasing power lost to the effects of inflation. While recent years have seen a settling of inflation rates at the 2-3% level, the combination of improving mortality and above-inflation increases in health care and long-term care expenses underline the importance of mandatory indexation.

We note the fact that, for example, the Ontario PBA provides for the concept of mandatory indexation. We believe such a provision, with a stipulated rate or range, should be enacted in the PBSA.

Disclosure of Plan Information

One of the primary means by which sponsors continue to exercise unequal power over pension plans is through their control over information. The disclosure rights established in the PBSA are crucial to member and retiree decision-making. CUPE continues to find that employers are reluctant to provide members with meaningful information about their plan, including the documents that they are required by law to provide. For example, too often we find that contribution holidays are denied or disguised. Benefit improvement possibilities (including indexation) are suppressed or needlessly deferred. And, when deficiencies emerge, the close relationship between employers (and employer agents) and plan agents leads to the presentation of selective menus of "solutions" to funding problems being presented to plan members – often by the authoritative and ostensibly independent plan actuary. This selective communication of plan financial and legal information to plan members by employers (and even Boards of Trustees) demonstrates to us that the letter and spirit of the minimal disclosure provisions of the PBSA are too often evaded, ignored, or insufficient.

CUPE would like to see the PBSA require far more disclosure of plan information by employers and plan administrators. All documents that must be provided to OSFI should also be automatically provided to any plan member on request (rather than provided "for viewing" at the workplace). Automatic provision of these same documents to all trade unions representing plan members should also be mandatory.

To facilitate providing this information, we support the Discussion Paper's proposal that information be made available through electronic means.

Beyond these general expansions of disclosure rights, CUPE has two additional specific proposals to make. First, employers and administrators are already required to report their application of surplus to "employer current service cost" (i.e. partial or full contribution holidays) to the regulators through reporting. Unfortunately, this crucial document – though technically available "for viewing" – is almost never provided to plan members or their trade union representatives. It would be a simple and cost-free improvement to the disclosure rules to require that the funding information reported in the normal filings also be included in the annual statement sent to all plan members. We see no good reason to deny this information to plan members when it is being annually reported to the regulators.

Second, we would suggest that plan disclosure rights could be easily enhanced through a requirement that employers and administrators provide pension committees and/or plan

member trade unions with copies of draft (not yet filed) actuarial valuation reports that report “excess surpluses” under the terms of the current ITA. It should be made clear to plan member trade unions or other representatives that the ITA “requirement” of employer contribution holidays to eliminate “excess” surplus is only triggered upon the filing – not the preparation – of a valuation that shows it. At the very least, plan members should be provided with an opportunity to propose alternatives to contribution holidays.

Along with these two specific disclosures, CUPE also supports the Discussion Paper’s suggestion that both missed payments and all contribution holidays be reported in a timely manner to members.

Discount Rates and Other Actuarial Assumptions

The Discussion Paper also discusses the actuarial assumptions or standards applicable to solvency calculations and in particular the determination of the discount rate applicable to valuing liabilities on a solvency basis.

In general, CUPE supports the current method to determine discount rates employed by the Canadian Institute of Actuaries. This method sets an interest rate with reference to a realistic cost of annuities in the Canadian market. This market-based method is the most appropriate method given the purpose of a solvency valuation, that is, to estimate the liabilities of a plan at a point in time. We also note that the requirement to base a discount rate on an annuity price from a regulated insurer is the most appropriate assumption given the nature of the defined benefit promise, which is to provide an annuity to members upon retirement.

Employing other discount rates is not appropriate. Some stakeholders have suggested that, for example, discount rates be based on corporate bond rates. This proposal is imprudent and inappropriate pension policy. Defined benefit plans do not promise corporate bonds, but life annuities. Solvency measurements should be defined to be as close as possible – with realistic margins – to that promise.

Current corporate bond rates, even very safe corporate bonds, are currently approximately 2-3% above available annuity rates. Discount rates based on those bonds would effectively create surpluses in most pension plans, notwithstanding the worst years in capital markets since the 1930s. It is fundamentally unsound to base solvency calculations on such unrealistic reflections of plan experience.

CUPE supports examining other ways to ensure a more adequate and less costly supply of annuities in the Canadian market, with consequent changes for the discount rate. We note that the Ontario Expert Commission on Pensions has also made such a recommendation. We submit that addressing the root problem – the price and supply of annuities – is the appropriate policy response to issues with the discount rate.

VI. JOINTLY GOVERNED PLANS

Improved and Joint Governance

CUPE is a strong supporter of improved pension plan governance. We participate in plan governance in various ways, including through collective bargaining, as participants in Jointly Trusteed governance arrangements, and in our general defence of plan members’ pension rights. Yet, while we feel we play a positive role in the enforcement of existing pension law, we consider it a weakness of the existing PBSA that the role of trade unions is not

specified and developed in more detail. This is a particular problem in light of the evidence showing the importance of collective bargaining agents in establishing and governing defined benefit plans.

In addition to the disclosure rule enhancements mentioned above, we would suggest that the plan member representation role of trade unions should be enhanced and empowered. In situations of significant plan change, such as partial or full wind-ups, divestments, “excess” surplus dispositions, benefit changes, governance changes, plan member trade unions can play a constructive role in negotiating the resolution of problems and communicating outcomes to members. However, to play this role effectively, the PBSA needs to spell out clear authorities and responsibilities.

On the other hand, CUPE also has experience with problematic plan governance and administration as a result of an unclear allocation of fiduciary duties and rules around conflicts of interest of plan agents. For example, we frequently find key plan agents – such as the plan actuary – being used by employers as their de facto representative, even within adversarial collective bargaining relationships. This strikes us as a clear conflict of interest for plan actuaries whose work is paid for out of plan resources, and who – we feel – owe a fiduciary obligation to the plan members. We would suggest that all plan agents owe fiduciary obligations to plan members.

To provide just one recent illustration, a CUPE Local with a single-employer negotiable pension plan was involved in collective bargaining over their plan in 2006. Within that bargaining, the plan actuary played a very aggressive and partisan role, advocating the employer’s position and refusing to answer straightforward questions posed by the union. The union complained to both the employer and the actuarial firm. While the employer ignored the complaint, the actuarial firm investigated the complaint and concluded that their actuary had, in fact, behaved unprofessionally and inappropriately. To their credit, they acknowledged the problem, and committed to ensuring it would not be repeated.

The point of this example is that we should not have had to file this complaint. Employers, actuaries, and trade unions should all be provided with very clear guidelines – set out in the legislation itself – regarding the fiduciary duties of plan agents and the avoidance of such conflicts of interest. We are aware that many employers with less informed trade unions – or no trade unions – are utilizing plan agents in exactly this fashion, and face no accountability in this regard. This is one of the most direct ways that employers – who are often deciding on the retention of plan agents – wield unfair power over plan members.

We are greatly encouraged that the Province of Québec has recently amended their pension legislation to clarify these fiduciary obligations of plan agents.

Multi-Employer Pension Plans and Jointly-Sponsored Pension Plans

CUPE also supports express statutory recognition of multi-employer pension plans (“MEPPs”), and a division of the PBSA devoted to special issues arising in the establishment and administration of MEPPs.

CUPE also urges the Government to create a new category of pension plan, called “jointly-sponsored” pension plans. These are currently recognized in Ontario. These plans are jointly sponsored by members and employers, and feature joint governance and joint responsibility for funding.

CUPE believes that this form of plan design and governance is an effective way to combine flexible regulatory standards while addressing issues of surplus use, volatility in contributions and information asymmetries inherent in the employment relationship. Existing jointly-sponsored plans in Canada are leading examples of the best performing pension plans.

With respect to both these special forms of pension plans – which co-incidentally, contain more members than all other forms of pension plans combined in Canada – should also have funding rules that are appropriate to their jointly-governed structures. The primary feature of these funding rules should be exemption from solvency funding.

The rationale for this exemption is primarily that members themselves are able to negotiate and accept risks taken on by the pension plan. Other supporting rationales are that, in multi-employer plans, there is a very low incidence of plan termination or wind-up, due to the multi-employer arrangement, and there is an ability to reduce benefits in the event funding remains inadequate to meet liabilities. As a result, solvency valuations are useful for information, but not as appropriate for setting contributions or funding policy. There is a similar rationale for public and broader public sector plans.

However, the primary consideration is that members participate in governance, and can make informed decisions, supported by expert advice, about the risks they are taking with their pension plans.

Structure of the PBSA

CUPE supports the re-organization of the PBSA into divisions applying to (i) all plans (ii) defined benefit plans (iii) defined contribution plans (iii) jointly sponsored and multi-employer plans, and (iv) single-employer plans.

Flexibility in the PBSA

In general, CUPE supports legislation that recognizes different plan designs and facilitates their use. However, we strongly believe that, to the extent pension regulation “encourages” the use of plans, defined benefit plan designs, or those substantially similar to them, should be a priority. By the same reasoning, we do not support legislative or policy initiatives that would further erode participation in defined benefit (or similar) plans.

In particular, CUPE supports the creation of “member-funded” pension plans as proposed by the Discussion Paper.

We urge the Government to consider creating categories of pension plans whose participants need not be employees, but members of some other recognized affiliation. These might include professional associations or similar communities of interest.

VII. DEFINED CONTRIBUTION PLANS

Preliminary Comments

As a general principle, we propose that defined benefit plans be subject to certain minimum standards applicable to all plans under the PBSA, but also subject to a division of the PBSA dedicated to issues arising only in defined contribution plans.

Safe Harbour Defences

The Discussion Paper proposes introducing a “safe harbour” rule that would provide a statutory defence to liability for breach of fiduciary duty in the provision of investment advice to employees. The rationale behind introducing this defence is to encourage sponsors to provide less conservative investment advice to employees, which may result in higher returns (and higher risks) to individual account holders.

We do not believe that the introduction of a statutory defence would significantly alter the quality of investment advice provided to employees. In fact, we do not believe it would alter that advice at all. As a result, no appropriate public policy objective would be achieved by this reform.

The Discussion Paper cites the use of a safe harbour rule in U.S. pension legislation. There is no evidence in the U.S. (or elsewhere to our knowledge) that this rule has enhanced the quality of investment advice provided to employees, nor is there any evidence that the safe harbour rule has increased returns to account-holders.

Providing a statutory defence to breach of fiduciary duty is also a significant intrusion on the “private” nature of occupational pension arrangements, substantially altering rights in favour of plan sponsors. Such an intervention into private arrangements should not be taken unless there is a clear public policy benefit and a balance of stakeholder interests.

A much more appropriate regulatory reform to meet the objective of improving employee investment advice and outcomes would be to require certain minimum standards be met by defined contribution plans. We also submit that regulation consider including the following elements as minimum standards in the provision of DC plans:

- A “know your client” rule akin to those used in securities regulation;
- Automatic adjustments to contributions over time;
- Automatic adjustment to asset mix in portfolios upon certain age thresholds;
- Full, plain and true disclosure of fees and a clear description of their impact on investment returns over time;
- Full disclosure of investment risk and discount rate risk to account holders; and
- A projection of benefits that would be obtained under standard investment scenarios, including the effect of investment and discount rate risks.

None of these standards require establishing a safe harbour defence. Rather, they help guide plan sponsors and service providers in the appropriate provision of defined contribution plans.

Standard of Care

The Discussion Paper proposes to modify the standard of care applicable to administrators (and agents) of defined contribution pension plans from a “fiduciary” to a “good faith” standard. The rationale behind this change is to encourage employers to provide defined contribution plans who might otherwise provide Group RRSP plans.

CUPE strongly opposes this proposal for several reasons.

First, the rationale provided by the Discussion Paper is incomplete in several respects. Administrators of defined contribution plans exercise considerable control over the plan design and implementation. Although they do not retain investment risk, which is partially borne by plan participants, they do retain discretion over all other elements of the creation and administration of the plan. In this respect, they are administrators who hold powers over the interests of others, they have discretion to affect those interests, and the plan members are in a position of vulnerability with respect to the plan administrator. These are the fundamental and long-standing hallmarks of a fiduciary. Consequently, we believe that plan administrators should be held to the standard of a fiduciary.

Second, we believe that to the extent that new pension plans should be “encouraged” by pension regulation, the priority should be defined benefit plans, not defined contribution or Group RRSP plans. There is ample evidence to show that, over time, defined benefit plans are better value propositions.

Third, reducing the standard to which plan administrators be held accountable cannot, conceptually and empirically, improve governance of pension plans. On the contrary, it reduces the standard of care to which an administrator will be held, which implies poorer governance.

Fourth, introducing two standards of care, one for defined contribution plans and one for defined benefit plans also invites a regulatory “race to the bottom”, both within and between jurisdictions. Sponsors will be incented to convert to defined contribution plans to take advantage of lower regulatory standards, and pressure will be put on other jurisdictions to do the same. Neither of these are appropriate policy objectives. If the difference in regulatory standards is indeed a motivating factor in the decision to sponsor a defined contribution plan – which we contend it is not – then the appropriate policy response is to regulate Group RRSPs under the same standards as defined contribution plans.

Surplus in Hybrid Plans

We have stated our position with respect to the entitlement to surplus above.

We submit that the principles articulated earlier also apply to the use of surplus in hybrid plans, the so-called “cross subsidization”. Surplus is the property of the plan to be used for the benefit of the members and retirees. It should not be diverted for use in contribution holidays or “cross subsidization” of employer contributions to a defined contribution plan.

There are further reasons to prohibit this practice. As the Discussion Paper states, defined contribution and defined benefit plans have fundamentally different benefit structures. Indeed, the Discussion Paper proposes applying different standards of care to these plans. Defined contribution plans are a significantly different pension promise. Conversion to a defined contribution plan is a fundamental change in the pension and in the terms of employment. As such, it is not an appropriate public policy to treat these plans as equivalent in the use of surplus arising in defined benefit plans. Surplus arising in a defined benefit plan should be used for the purposes of the defined benefit plan, and not other sponsor uses, or for contributions to a defined contribution plan.

VIII. CONCLUSION

CUPE greatly appreciates this opportunity to address several of the issues raised by the Department’s Discussion Paper and overall mandate. We look forward to presenting our views in person, and would be happy to answer any questions that may arise from the foregoing.

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