

**DISCUSSION PAPER**

**Submitted to**

**The Department of Finance Canada**

**Discussion Paper on Private Pensions**

**Submitted by:**

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## Introduction

On January 9, 2009, the Department of Finance, Canada issued a Discussion Paper on Private Pensions and invited responses from Canadians. This is my response.

I will not cover all of the topics introduced in the Discussion paper. In fact, I will focus mostly on Section 5. A. Issues Respecting the Framework for Private Pension Plans. You state: *“The Government is seeking views on whether there is interest in alternative plan designs that may not currently be accommodated by the legislative framework.”*

My second focus will be Section 5.B. Multi-Employer Pension Plans where: *“The Government of Canada is seeking views on whether there are legislative impediments to the creation or operation of multi-employer pension plans, and if there are improvement that could usefully be made to the legislative framework for these arrangements”*.

I will include a minor discussion on Section 3.D. Disclosure of Information.

In the past two years, several Discussion papers have been created. These include:

The Member-Funded Pension Plan from the Regie Des Rentes Du Quebec;

Promises to Keep, The Nova Scotia Pension Review Panel;

Getting our Acts Together: the Alberta/British Columbia Joint Expert Panel on Pension Standards; and

A Fine Balance: Safe Pensions, Affordable Plans, Fair Rules: the Report of the Ontario Expert Commission on Pensions.

These reports in total represent hundreds of pages of carefully thought-through positions. Clearly, four separate and independent sources of opinion could not agree in detail about the future evolution of Canadian pensions. However, I have been struck by the strong similarities of the intent of their major recommendations.

In this short paper, I hope to convince the reader that these four reports have a great deal in common especially if we allow ourselves to review only their major recommendations (although, admittedly, one can argue about what is major and what is not) and if we allow ourselves to view the recommendations from a lofty level so that we can see the trees and not just their branches (and maybe even the forest!).

My process is simple. I have reviewed in detail the four reports referred to above. I now wish to summarize their findings in a limited number of categories to convince the reader of the amazing commonality of intent in the major recommendations.

Because I am addressing experts in the field, I leave many minor points and definitions unstated.

### **The Member-Funded Pension Plan from the Regie Des Rentes Du Quebec**

The Member-funded Pension Plan (MFPP) is a Defined Benefit (DB) target benefit (TB) plan. The plan is intended for companies that have a Collective Bargaining Agreement (CBA) unless waived by the Minister of National Revenue.

For the employer/plan sponsor, this plan is a Defined Contribution (DC) plan. All responsibility ends once the required contribution is made. For the employees, the risks inherent in a pension plan (well know and not to be reiterated here) are mitigated through the collective nature of the scheme versus an Individual Account DC plan.

If there are more than 25 members, the plan is expected to have a pension committee. This committee must know and understand the plan obligations for members and any changes in these.

Indexation of benefits, both before and after retirement is contingent on the funding health of the plan.

A MFPP can be a Multi-Employer Pension Plan (MEPP) or a Single-Employer Pension Plan (SEPP). The MFPP is meant to be fully funded at all times (remember that the indexation of benefits is contingent). To repeat, the MFPP is a target benefit DB plan.

### **Promises to Keep, The Nova Scotia Pension Review Panel**

The panel notes that the existing rules inhibit innovation in plan design and, thus, the creation of new DB plans.

It notes that Special MEPPs are DC plans for the plan sponsor and Target Benefit plans to the worker participant. Jointly-Sponsored Pension Plans (JSPPs) are Defined Benefit plans that have joint governance and contingent (target) benefits. For both SMEPPs and JSPPs, workers are an integral part of the decision-making process with respect to the plan. The panel suggests that the target benefit model could and should be utilized more broadly.

The panel would like to see decreased regulation balanced by transparency of information and either Joint Trusteeship or Advisory Committees. As one example, if the governance process can be strengthened, then specific investment limits can be removed. The administrator, sponsor and plan members should have access to relevant, timely and accurate information (and plan members include former members with deferred benefits and retirees). In fact, information provided to the Superintendent should simultaneously be provided to the Advisory Committee and employees. If the plan is not Jointly

Sponsored, then the Advisory Committee should have full rights to relevant pension information and plan professionals. The Advisory Committee should have at least one retired plan member. These Committees need orientation and training (an obligation of the plan sponsor).

It notes that employees do face several risks in a DB plan, including:

- the employer may cease to exist
- the plan may be terminated
- employees may be asked to raise contribution levels

The panel suggests that Nova Scotia should create a new Promotion Division to promote plans and provide support as outlined. This Promotion Division would be separate from the Superintendent.

Finally, the panel suggests the creation of a new Province-wide Plan. This plan would be open to all employers and employees and administered by an independent agency and would include workers with no plan today and the self-employed. The plan would accept commuted values for workers shifting jobs or if a plan terminates. Plan participation would be voluntary. The Plan would be a DC Target Benefit plan. The Superintendent could move poorly managed plans into the province-wide plan. A provincial agency would be responsible for administration and for investing the funds but not for any plan risks nor any costs of administration or investment management.

### **Getting our Acts Together: the Alberta/British Columbia Joint Expert Panel on Pension Standards**

The Panel recommends the creation of the position of a “Pension Advocate” who would be responsible for promoting pension coverage, generally identify barriers and work with stakeholders and government to develop solutions to key pension issues.

The Panel supports the concept of the creation of a Joint Advisory Council, comprised of individuals from a variety of backgrounds, to provide ongoing input and advice to the Ministers and the regulator(s) with respect to pension policy matters. The Chair of the Joint Advisory Council would be the Pension Advocate.

Standards should accommodate a wider variety of pension arrangements than were contemplated in the current statutes and should be tailored to the key characteristics of different types of pension plans—especially to the risks associated with those different types of plans.

Pension plans should be required to have a governance policy, which includes a funding policy if the plan contains a target or DB provision, and this should be disclosed to members including retirees. It should include an assessment of educational requirements and training needs for those who have responsibility for aspects of plan administration.

Individuals having statutory fiduciary responsibility should be required to complete training programs and receive a certificate.

Current rules imposing quantitative limits on investments should be repealed, making investments subject to the “prudent expert” standard .

The governments of British Columbia and Alberta should encourage the federal government to review all of the income tax limits related to pension plans. In particular, that the ITA limit on pension plan surplus should be raised to 125 percent of liabilities (except for IPPs).

Finally, the plans’ funded status would be measured and any adjustments made on a going-concern basis. The plans would no longer have to prove that their assets would cover liabilities in the event of plan wind-up (“solvency basis”).

The Panel recommended a new provincial ABC plan. The plan would be available to any employer, employee or self-employed person at a reasonable cost, enabling them to take advantage of the economies of scale afforded by pooling pensions risks and assets as well as access to investment expertise and products not currently available to small pension plans and individual investors. Administration and investment management should be competitively tendered. To be successful, total expense ratios for this type of plan, including investment management and administration expenses, should not be greater than 0.4 per cent of assets under management. The plan would be a simple DC plan, and enrolment would be automatic for employers and employees, who could opt out if they did not wish to participate. Self-employed people could participate by opting in (with the same tax advantages). Employees and employers would not have any discretion with respect to the investment of plan assets, which would be invested subject to the policy direction of the board of governors. Provision of annuities directly from within the plan (versus buying an annuity in the private sector) should be considered if the plan becomes large enough.

While full coverage is desirable, it is not feasible for two provinces to establish a mandatory plan. A mandatory program, to be successful, would have to be national in scope, otherwise the two provinces would be disadvantaged competitively compared to the rest of the country.

Support for auto-enrolment with opt-out stems in part from recent pension legislation in the United States and the United Kingdom where there has been an increase in pension plan coverage due to auto-enrolment design features (60% for auto-enrolment versus 42 percent for opt-in plans).

The majority of the board of governors would be experts.

## **A Fine Balance: Safe Pensions, Affordable Plan, Fair Rules: the Report of the Ontario Expert Commission on Pensions.**

The OECPC noted that the Ontario PBA is designed for SEPPs DB plans to protect the worker participant. But, if we assume that plans under CBAs, MEPPs and JSPPs do not need this level of protection, then the PBA regulates less than 20% of the workers who have employer-sponsored pension plans. And this percentage is in decline. This is nonsensical.

The PBA and ITA should allow and encourage plan innovation. Just the opposite is true today.

The Commission pointed out that size matters:

- Better financial advice at lower per unit cost,
- Lower Management Expense Ratios
- Broader investment vehicles (e.g., private placements),
- More spreading of risks (e.g., mortality, investment, interest rate),
- Enhanced levels of information, education and service,
- Lower administrative costs per unit.

The OECPC recommended the creation of a Pension Champion, a new government agency along with a new Pension Community Advisory Council which would include all stakeholders.

The Commission noted that the better the quality of governance for a plan, the less need there is for invasive regulation. Thus, we should improve the process, quality and transparency of decision making and facilitate greater participation in plan governance by active and retired plan members. The Pension Champion should lead efforts to provide better training for both professional and lay participants in plan governance and administration.

Plans should file with the regulator statements with respect to governance, funding and investment policies. Plans should provide more and clearer information to active and retired members and their authorized representatives including implications of the plan's funded status.

The OECPC recommended that the temporary rules for SOMEPPs (e.g., going-concern valuation) should be made permanent and extended to all MEPPs, all JSPPs and to the new Jointly-Governed Target-Benefit plans (JGTBPPs). JGTBPPs are to be encouraged. It is expected that they would exist in a workplace that has a CBA or the equivalent (e.g., a faculty association). Members of target benefit plans must be educated on all of the risks associated with this type of plan. Participation should be automatic. One would have to act to opt out.

Target benefit plans are DB but allow benefits to be adjusted upward or downward depending on the funding health of the plan. For the plan sponsor, these plans are DC. While these now exist for MEPPs, they are not available for SEPPs.

Under JSPPs or JGTBPPs, all plans should be required to establish Pension Advisory committees representing all constituencies of active and retired members, unless members vote against having one. These committees should have 50+% of their population from active and retired members of the pension plan. JSPPs and JGTBPPs would fund to a going-concern valuation and would not make PBGF contributions. In general, retirees should have full access to information and be eligible to participate in the plan governance process with active members.

The 110% surplus limit imposed by the ITA should be raised.

The Commission also proposed a change in legislation and regulations to encourage the commingling of small/medium size plans to achieve the advantages of size. Further, it recommended that the province should establish an Ontario Pension Agency for stranded pension assets. An alternative to a new provincially created plan would be to allow existing MEPPs and JSPPs to service new, less-connected, members. Models for such a plan would be the existing OMERS (Ontario Municipal Employees Retirement System) and TIAA-CREF (Teacher's Insurance and Annuity Association-College Retirement Equities Fund, which has 3.4 million members from 15,000 institutions and \$420B of invested assets). Another model would be the BC Investment Management Corporation (BCIMC). Affinity groups should also be able to form such commingled arrangements.

Management could be through a private agency (e.g., sponsored by the insurance industry) so long as total expenses were kept very low (e.g., less than 0.5% of assets).

The Commission recommended as an alternative the expansion of the Canada/Quebec Pension Plans (e.g., a voluntary second tier) or the creation of a comparable provincial plan.

## **Conclusion**

It is worth noting that this submission is really only six pages long.

What I have done in my submission is to summarize many of the major recommendations of four recent pension review panels (as outlined in the Introduction).

I have been amazed by how similar the intent of the major recommendations is and I hope the reader is similarly impressed.

When four independent and wise panels from five Provinces make such strong and similar recommendations, it seems to me there must be content worthy of further discussion.