



Joint Submission to Department of Finance Canada on its January 2009 Pension Plan Consultation Paper

Submitted by the Chief Financial Officers of Air Canada, Bell Canada,
Canada Post, Canadian National Railway Company, Canadian Pacific
Railway Limited, MTS Allstream and NAV CANADA

March 5th, 2009

INTRODUCTION

This submission to the Department of Finance is being made by the Chief Financial Officers (CFOs) of seven major federally-regulated employers in the transportation and communication industries, being:

Air Canada	Michael Rousseau
Bell Canada	Siim Vanaselja
Canada Post	Wayne Cheeseman
Canadian National Railway Company	Claude Mongeau
Canadian Pacific Railway Limited	Kathryn McQuade
MTS Allstream	Wayne Demkey
NAV CANADA	Brian Aitken

Our seven companies have been sponsors of Defined Benefit (DB) pension plans for decades. Currently, our defined benefit pension plans, all of which are registered under the Pension Benefits Standards Act (PBSA), collectively cover approximately 162,000 employees and provide pensions to over 145,000 retired employees and their beneficiaries. Our pension funds collectively hold approximately \$56 billion of assets (December 31, 2008), which represents approximately 60% of the assets of all of the defined benefit plans registered under the PBSA. Throughout the years, our defined benefit plans have delivered pension benefits to hundreds of thousands of Canadians without ever missing a payment. Over the last five years alone, our pension plans have collectively paid out approximately \$15 billion to our pensioners and their beneficiaries and other plan members.

FOUNDATION AND PRINCIPLES OF OUR SUBMISSION

We – the CFOs of our seven organizations – strongly believe that meaningful, permanent actions by the Federal Government are urgently required to address the onerous and volatile nature of the current solvency deficit funding rules for defined benefit pension plans. The current rules severely limit our companies’ ability to invest capital to enhance our infrastructure and grow our businesses, thereby adversely impacting not only our companies but also the Canadian communities in which we operate and the Canadian economy in general. Further, the current rules hinder our ability to compete in North American and global markets.

We believe that this submission is consistent with the principles outlined in the Consultation Paper, namely that:

1. The rules governing private pensions should be reflective of the voluntary and contractual nature of the arrangement;
2. Employees and retirees should have the necessary information to make informed decisions; and
3. The legislative and regulatory framework should ensure that certain minimum standards are met in order to ensure a level of benefit security for plan members.

**Joint Submission to Department of Finance Canada
On its January 2009 Pension Plan Consultation Paper**

We acknowledge the critical importance of the security of the benefit payments for the members of DB plans, but strongly believe that the best security for plan members is a financially strong plan sponsor.

This submission articulates our concerns and our proposals for changes to the current framework. Our proposals are presented as one cohesive package that is intended to be taken as a whole, and are consistent with the principles of balance, transparency and security that were outlined in the Consultation Paper.

There are some elements of the Consultation Paper that we have not addressed as a group – each of our organizations may choose to address these elements in their individual submissions.

We consent to this submission being posted on the Department of Finance web site and to a copy of this submission being forwarded to OSFI.

OUR OVER-RIDING CONCERN WITH THE CURRENT REGULATORY FRAMEWORK

All stakeholders recognize that the world has changed significantly since solvency funding rules were introduced in 1987. The members of our pension plans have become older (and are living longer), while the business world and financial markets have become more global, and certainly more connected. Our customers, our employees, our shareholders and the communities in which we operate all require that we be more competitive. Current pension laws and regulations severely and negatively impact that competitiveness. These factors combined with extremely volatile financial markets (as demonstrated by their recent rapid collapse and for which there is presently no end in sight) have made the current solvency funding rules far too onerous on sponsors and have undermined their competitiveness and productivity.

DB pension plans such as ours have played a significant role in the Canadian retirement income system, but today their survival is severely threatened. Without meaningful, permanent changes to the current solvency funding rules, our ability to maintain our DB pension plans will be seriously challenged.

The unnecessarily onerous and volatile solvency deficit funding rules are, without a doubt, creating an unwarranted crisis for companies that sponsor defined benefit pension plans.

- Our seven companies' aggregate pension contributions over the last four years have been large and volatile:

2005	\$1.2 billion
2006	\$1.7 billion
2007	\$0.8 billion
2008	\$1.0 billion

**Joint Submission to Department of Finance Canada
On its January 2009 Pension Plan Consultation Paper**

- Five-year funding of our seven companies' December 31, 2008 solvency deficits (with assets reflected at market value) would result in aggregate annual contributions of \$3.5 billion, an increase of \$2.5 billion over 2008
- Ten-year funding of these solvency deficits would result in aggregate annual contributions of \$2.4 billion, which would represent an increase of \$1.4 billion over 2008.

Despite the massive increase in contribution requirements for our collective pension plans, they remain reasonably well funded with the market value of our collective plans' assets equal to approximately 83% of their solvency liabilities as at December 31, 2008.

URGENT CHANGES REQUIRED TO SOLVENCY FUNDING RULES

It is critical that meaningful, permanent changes to the regulatory framework be made in 2009 to address the onerous and volatile nature of solvency deficit contributions required under the current rules.

We are requesting that the solvency deficit amortization period be permanently increased from five years to 10 years for all current and future solvency deficiencies, without any conditions.

It is imperative that this longer amortization period be provided without any conditions.

- Requiring member consent in an area as complex and sensitive as pension benefit security requires a complicated and difficult communication process that will be impractical for most plan sponsors to implement. As well, it is a process that will inevitably create tensions which are attributable to the current funding rules being excessively onerous.
- Letters of credit (used to provide security under the temporary solvency relief measures) are no longer an inexpensive, readily accessible means of securing pension benefits. Letters of credit can, however, serve as a pragmatic approach to addressing risk/reward asymmetry in DB pension plans, as discussed later in this submission.
- What is required is certainty, predictability and clarity – a permanent fix to get away from a continual cycle of temporary relief measures.

The existing Regulations under the PBSA permit the solvency deficit amortization period to be so extended, thereby permitting this change to be enacted promptly without waiting for the enactment of the Government's proposed PBSA amendments. We urge the Government to make this change during 2009, since companies require more certainty around future years' pension contributions as they proceed with the development and implementation of their corporate capital and operating plans.

IMPORTANT ELEMENTS CONCERNING SOLVENCY MEASUREMENT

We are seeking changes to three elements of how solvency liabilities are determined:

1. Discount rate. Our companies have, over the last several years, expressed concerns with respect to the conservative nature of the discount rates used to calculate solvency liabilities for both active and retired members. We have been working with the Canadian Institute of Actuaries (CIA) to address these concerns. We are encouraged by recent developments, namely the CIA's new commuted value standard and the recognition by the CIA, with OSFI's concurrence, that large and/or indexed pension plans cannot immediately settle their obligations by purchasing annuities.

Given this recognition by the CIA and OSFI, it is important for the Government to take leadership in prescribing a discount rate for solvency liabilities that is better aligned with the marketplace. We recommend that the Government introduces a regulation to prescribe the discount rate based on a benchmark AA corporate bond index.

In the meantime, it is imperative that OSFI continue to exercise its judgment and discretion, based on the recently adopted CIA standards, especially for large and/or indexed plans such as ours.

2. Asset smoothing. We emphasize the importance of continuing to allow sponsors to retain asset smoothing methods for solvency funding purposes, to mitigate the contribution volatility resulting from the mark-to-market nature of the solvency funded status. We believe that the Government's Budget 2009 announcement that introduces a deemed trust requirement if a smoothed asset value exceeds 110% of the market value is an unnecessary complication, as asset smoothing methods are, by their very nature, self-correcting over short periods of time. We believe that OSFI should accept caps higher than 110% without a deemed trust applying.
3. Indexed plans. For pension plans that contain automatic inflation indexing provisions, the calculation of solvency liabilities is especially burdensome. We believe that the best way to address the untenable situation faced by sponsors of indexed plans is to exclude indexing from the calculation of solvency liabilities when determining solvency amortization payment requirements. Funding of the indexed benefits, including deficit amortization, would continue to be provided through the going-concern funding valuation (which more closely matches the period of funding to the long-term nature of this portion of the pension liability). This proposed change, which is consistent with provisions that have been in effect in Ontario and Nova Scotia for more than 15 years, would greatly facilitate the maintenance of automatic inflation indexing provisions in private sector plans.

PARTIAL PLAN TERMINATIONS

We support the elimination of the concept of partial plan terminations from the PBSA. In exchange, we propose that pension benefits fully vest after one year of plan membership (as opposed to two years at present). One year vesting (as opposed to immediate vesting as proposed in the Consultation Paper) is a compromise that reflects the small benefit value that typically applies for members who terminate with less than one year of plan membership versus the administrative costs associated with processing vested benefits.

RECOGNIZING THE NEED FOR A BALANCED APPROACH TO STRENGTHEN THE LEGISLATIVE AND REGULATORY FRAMEWORK

We recognize the need for a balanced approach for strengthening the legislative and regulatory framework. In return for meaningful, permanent solvency funding adjustments, our seven companies support the following changes in the regulatory framework:

1. A requirement for plan sponsors to fully fund any deficit on plan termination (with such funding either, at plan sponsor discretion, made in a lump sum or amortized over a period of up to five years). It is imperative that the outstanding obligation be treated as unsecured debt of the sponsor and not rank ahead of any of the sponsor's other unsecured debt.

We would support provisions that would allow a plan to be terminated in an underfunded position by virtue of an agreement between the sponsor and the plan members. With respect to member consent thresholds for such an agreement, we suggest that the Government adopt the member consent provisions contained in the 2006 temporary solvency funding relief regulation.

2. A requirement that plans must file actuarial valuation reports annually with OSFI, irrespective of the plan's funded status. Removing the ability for a plan sponsor to continue to take a contribution holiday for another year or two as if the plan still has a surplus, when in fact the markets may have dramatically deteriorated, will have a material beneficial impact on benefit security once the markets recover and surpluses return.
3. Greater disclosure to all plan members of the plan's funded status, the plan's investment policy and a statement of funding policy. The statement of funding policy should address the sponsor's policy with respect to contribution holidays, but should refrain from addressing those funding issues which are linked to the sponsor's management of the financial risks associated with the operation of its business and are typically reserved for decision by the sponsor's board of directors and therefore considered confidential.
4. A prohibition on plan improvements if a plan is less than 85% funded on a solvency basis (or if the improvement would result in the funded status dropping below this 85% threshold).

5. An increase in the current Canada Revenue Agency “excess surplus” limit on employer contributions above its current 10% surplus threshold to 25%, thereby giving employers the option to pre-fund cyclical market downturns.

ADDRESSING RISK/REWARD ASYMMETRY

The Consultation Paper only indirectly seeks comments regarding risk/reward asymmetry (attributable to plan sponsors being solely responsible for any pension deficits while their access to surplus is restricted). Although surpluses may appear remote at the present time, the conservative nature of the solvency liability calculation, together with the required amortization of solvency deficits, ensures that trapped capital and risk/reward asymmetry issues will emerge at a future date. We encourage the Government to address these issues at the present time.

A practical approach to addressing trapped capital and risk/reward asymmetry is to permit plan sponsors to use letters of credit in lieu of solvency contributions, to the extent that these contributions exceed going-concern deficit contributions. The letters of credit must be permitted to be reduced or canceled if a solvency surplus later develops. We note that Alberta and British Columbia have adopted this approach on a permanent basis.

For letters of credit to be effectively utilized for this purpose, they must be an alternative source of funding that sponsors can voluntarily utilize. They cannot be a trade-off for lengthening solvency deficit amortization periods for the reasons outlined earlier in this submission.

We request that the Government permit sponsors to utilize letters of credit for this purpose.

We understand that other organizations may be proposing to Finance that solvency valuations include a provision for adverse deviations (PfAD), and that, as a minimum, no contribution holidays be permitted until the plan’s assets exceed the plan’s solvency liabilities by an amount equal to the PfAD. Our companies believe strongly that such a PfAD is not appropriate unless the PBSA were to be amended to provide plan sponsors with clear entitlement and access to surplus assets.

CONCLUSION

We support the need for a balanced approach that will provide an acceptable degree of funding flexibility for sponsors and both transparency and pension benefit security for plan members.

With the continuing lack of liquidity in the capital markets and the continuing decline in equity markets in early 2009, and with the need for companies to plan now for their increased pension contributions over the next several years, it is critical that these issues be urgently addressed. The proposals that we have made in this paper would free up billions of dollars over the next several years to be productively invested within our businesses for the benefit of all of our stakeholders as well as the communities in which we operate.

We believe that our proposed solution provides an appropriate level of balance.

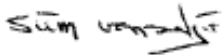
**Joint Submission to Department of Finance Canada
On its January 2009 Pension Plan Consultation Paper**

We look forward to the opportunity to continue our dialogue with the Department of Finance.

Respectfully submitted,



Michael Rousseau
Executive Vice President and Chief Financial Officer, Air Canada



Siim Vanaselja
Executive Vice-President & Chief Financial Officer, Bell Canada



Wayne Cheeseman
Chief Financial Officer, Canada Post



Claude Mongeau
Executive Vice-President and Chief Financial Officer, Canadian National Railway Company



Kathryn McQuade
Executive Vice-President and Chief Financial Officer, Canadian Pacific Railway Limited



Wayne Demkey
Chief Financial Officer, MTS Allstream



Brian Aitken
Vice President, Finance, Chief Financial Officer and Treasurer, NAV CANADA