December 21, 1999

Recommendations

of the

ACPM, PIAC, OSFI Joint Task Force

on

Pension Plan Governance and Self-Assessment

Recommendations of the

ACPM, PIAC, OSFI Joint Task Force

on

Pension Plan Governance and Self-Assessment

Contents

ACPM, PIAC, OSFI Joint Task Force on Pension Plan Governance and Self Assessment

Recommendations

Introduction

The Standing Senate Committee on Banking, Trade and Commerce issued a Report on The Governance Practices of Institutional Investors in November 1998. This Report included a recommendation that pension plans in Canada adopt industry best practices with respect to plan governance. Specifically, the Committee recommended that plan administrators "adopt one of the PIAC, ACPM or OSFI guidelines and report annually to pension plan members setting out how they comply with, or exceed, the adopted set of guidelines, and explaining why they do not comply if they choose not to do so."

The Committee intends to hold hearings in the year 2000 to determine whether regulations are needed to ensure that plans are well governed, or whether voluntary compliance with the guidelines, together with reporting to plan members, has proven satisfactory. The recommendation also noted that "implementation of this recommendation should proceed once the three organisations are prepared to provide assistance to their respective stakeholders who need guidance on how a plan is to perform self-assessment."

Since the three guidelines issued by PIAC, ACPM and OSFI in the past few years contain many common principles, these organizations have formed a Joint Task Force on Pension Plan Governance (the "Task Force"). Its purpose is to develop a common set of pension plan governance principles and a guide for plan administrators to conduct an assessment of their governance practices.

The Task Force participants are:

ACPM — Association of Canadian Pension Management representing a thousand members which includes small, medium and large pension plan sponsors and industry consultants (Gretchen Van Riesen, Michael Beswick and Bruce Tollefson).

PIAC — Pension Investment Association of Canada representing some of the largest pension funds in Canada (Don Walcot and Bob Bertram).

OSFI — Office of the Superintendent of Financial Institutions (Canada) which regulates some 1,100 pension plans across Canada (Ron Bergeron and Pirjo Davitt).

The Task Force started with the following beliefs:

- An effective system of governance considers all facets of pension plans, such as funding, investment, benefits administration, and management, and is essential for all types and sizes of pension plans, including defined contribution plans and MEPPs.

- Governance issues would benefit from greater exposure and publicity. Plan administrators need to better understand what governance means and how it relates to their obligations to plan beneficiaries, and to their statutory and fiduciary responsibilities.

- Some form of governance evaluation is essential for plan administrators in understanding the governance risks they and their plans face, and where improvements are required. This may be accomplished through a self-assessment process.

- Governance structures and practices are being established in many pension plans. Even smaller plans are responding to this need.

- Understanding of governance and self-assessment are continually developing and will evolve over time.

Objectives of the Task Force

The Task Force has three primary objectives:

- To develop a set of governance principles which can be adopted by all types and sizes of pension plans across Canada; and thereby increase the effectiveness of governance practices of pension plans and increase protection for plan beneficiaries.

- To develop a cost-effective self-assessment and reporting regime, focused on high level issues rather than processes, that will be flexible and applicable to all pension plans.

- To raise the level of understanding of plan administrators concerning their accountability for decisions and actions affecting the pension plan and the delivery of the pension benefits.

The Task Force believes that if these objectives can be realized, plan beneficiaries and administrators will achieve significant benefits, without the need for increased regulation.

Why Governance?

See Appendix 1 for benefits of effective pension plan governance.

Governance Principles

The principles of pension plan governance are listed in Appendix 2, along with a brief commentary on each.

The Pension Plan Governance Self-Assessment Questionnaire

A self-assessment tool is provided in Appendix 3, along with instructions for its use.

Further Assistance for Plan Administrators

The ACPM, PIAC and OSFI have each posted these recommendations, in addition to their governance guidelines, on their web sites:

ACPM	acpm.com
PIAC	piacweb.org
OSFI	osfi-bsif.gc.ca

Conclusion

Pension plans in Canada are at a cross-roads with respect to governance. Effective governance is increasingly recognized as an essential feature of a well run pension plan. While many plans have paid attention to this need, many have not. A variety of governance approaches have been tried, and ACPM, PIAC, and OSFI have discussed governance principles in their published guidelines, yet the subject remains murky in the minds of many pension administrators. However, the alternatives to improved plan governance may be increased litigation, more involvement by regulators in the operations of plans, and more prescriptive regulations.

The Senate Committee Report has given a new impetus to the idea of that each plan should adopt a governance standard appropriate to its particular requirements. The opportunity exists for pension plans in Canada to move to the next level in their development by considering the principles and the assessment tool developed by the Task Force and implementing the principles in a way that is best suited to each plan’s circumstances.

Why Governance?

An effective governance system is a good method of overall risk management. Controlling the legal and other risks facing plan sponsors and plan fiduciaries is only one reward for good governance practices. Indeed, benefits of effective governance also include improved investment performance, better use of time for plan sponsor and pension plan personnel, and reliable assurance to members that the plan is able to pay benefits presently and in the future. In addition, governance self-assessment that leads to improved plan governance practices will prevent the need for additional government regulation.

Defined Contribution Plans

While the principles of good governance apply to all types and sizes of pension plans, defined contribution plans deserve particular mention. Some plan sponsors have assumed that governance responsibilities are diminished or eliminated because investment risk is shifted to plan members under a defined contribution plan. There are, however, a number of topics requiring attention from a governance perspective — such as the selection of investment options offered to members, the investment performance of these options, and the education and communication program for members. In addition, the governors should have processes for assuring themselves that such areas as plan administration, remittance of contributions and payment of benefits comply with applicable legislation and with the plan's terms. Group RRSPs, while not subject to pension plan legislation, should also be governed by principles similar to defined contribution plans.

Self-regulation

Some pension regulators are moving to a self-regulating regime. This means responsibility for safe pension benefit delivery is shifted from the regulator to the other pension industry stakeholders: the plan governors, administrators, managers, sponsors, employers, unions and employee associations, advisors, financial institutions, and plan members. In the past, many plan sponsors have relied upon regulators to advise them when their plans were not compliant with applicable legislation. In a self-regulatory environment each stakeholder is accountable to the others for keeping the industry viable. In this environment it is important to know whether each stakeholder is doing a good job. The Pension Plan Governance Self-Assessment Questionnaire assists plan governors in assessing their own performance and determining where weaknesses exist that require corrective actions.

Self-assessment offers an opportunity for plan sponsors to share responsibility for the pension benefit delivery with the other stakeholders. Transparency of information about existing conditions, decisions and actions is integrally related to accountability. Reporting the self-assessment results (e.g., to the Board of Directors of the sponsoring employer, to each participating employer and union in a MEPP, and to plan members) provides accountability to interested stakeholders instead of the regulator. Therefore, the Task Force considers that reporting findings and action plans to other interested stakeholders is an industry best practice, and recommends that regulators receive or request governance self-assessment results only where there is some reason for concern over the governance of a plan. In fact, OSFI has indicated its intention not to routinely request governance self-assessment results.

The Regulator's Role

The experience of regulators with the governance of underperforming plans underscores the need for appropriate levels of accountability and checks and balances within each pension plan. Governance problems are demonstrated, for instance, through confusion about responsibilities and expectations, inability to deliver pension benefits, mismanagement of pension assets, and legal actions against parties involved in plan and fund governance.

While regulators are attentive to any warning signs of poor management, use of the self-assessment tool by a pension plan shows appropriate prudence. One purpose of this package is to help plan governors and administrators to be better prepared should a regulator or any other stakeholder ask about the plan's governance. Sound pension plan governance considers the interests of all stakeholders and eases the work of a regulator.

Future

The Task Force intends to assess the effectiveness of the Pension Plan Governance Self-Assessment Questionnaire in the future by conducting a "no name" survey of how many plans are using it, what more is needed, who is being informed of results etc. In the meantime, we urge plan governors to become better educated about pension plan governance and governance self-assessment, risk management, and information sharing in a self-regulatory environment.

Pension Plan Governance Principles

Though the Task Force feels that the basic principles of governance apply to all pension arrangements, we have addressed registered pension plans in particular. The principles listed below cover all aspects of delivering the benefits promised by a pension plan, including pension administration, as well as funding and investments, and apply to all types and sizes of pension plans, including defined contribution plans and MEPPs.

These principles are ones which, in the opinion of the Task Force, are essential to achieving effective governance of a pension plan. There can be many methods for implementing these principles. The value of good governance comes from reflecting on each and taking a considered stance.

Principle	Discussion
1. Pension plans should have a clear mission	• The plan's mission defines why the plan exists. It will likely reflect the plan sponsor's reasons for establishing and maintaining the plan. It should be clearly distinct from company/union mission statements. • The mission statement facilitates the adoption of measurable goals against which the plan's and its governors' and administrator's performance is measured.
2. Pension plans have a primary fiduciary duty to plan beneficiaries	• Pension plan governors and administrators owe a duty of loyalty to the plan and its beneficiaries over and above any constituency interests. • A code of conduct, including conflict of interest policies and procedures, covering benefits administration and funding, as well as investments, should be clearly articulated and monitored.

3. Responsibilities/accountabilities should be allocated clearly in order to: • identify stakeholders • allocate responsibilities • define roles	• The plan's governors and administrators should define the responsibilities of each participant in the governance, management and operations of the pension plan, and clearly identify the stakeholders to whom each are accountable. • Accountability is enhanced through disclosure and transparency. E.g. the Board of Directors or Board of Trustees may delegate their responsibility for paying benefits correctly to a Pension Committee, who in turn may assign this authority to senior officer(s), who in turn may assign it to a more junior officer or to an external agent. The Board of Directors' or Board of Trustees' responsibilities are not transferred by this delegation, and thus they should have supervisory processes in place. In small plans, there may be a smaller number of parties involved, but the principle of allocating responsibilities and accountabilities remains the same.
4. Performance should be measured and reported	• The plan's governors should measure performance, including pension administration and funding status as well as investments, against pre-defined goals, adjusted for differing needs over time. • Measuring performance facilitates the separation of the supervision of operations from their execution. • Performance objectives and measures should be tailored to each plan's specific requirements. • Results should be reported to the appropriate stakeholders.
5. The pension plan administrator should be qualified and knowledgeable	• Each person involved in plan administration should have, or acquire, knowledge and skills that are current and appropriate for the responsibilities and accountabilities they carry.
6. Governance self-assessment	• The governance process should be reviewed and modified over time to ensure its effectiveness, with reporting to the appropriate stakeholders.

Definitions of Terms

"Administrator" refers to all persons and bodies associated with the plan (and their agents) who have either governance, management or day-to-day operational responsibilities over matters affecting the benefit entitlements earned by plan members and beneficiaries.

"Governor" refers to persons and bodies with the highest level of plan governance authority according to the terms of the plan or applicable legislation (e.g., the plan sponsor's board of directors, the MEPP board of trustees). It will usually also include a committee which has responsibilities for the plan and its members.

"Stakeholder" refers to parties who have an interest in the outcomes of the decisions and actions regarding the plan. It includes plan members, plan governors, administrators, managers, sponsors, employers, unions and employee associations, advisors, financial institutions, and governments.

Appendix 3

Pension Plan Governance Self-Assessment Questionnaire

Completion of the questionnaire

The Task Force hopes that this questionnaire will be a useful tool for pension plan governors and administrators to commence assessing their own plan's performance, and recognizes that it is not suitable for formal and rigorous self-assessment. The responses should honestly reflect the situation of the plan, and will thus point out areas that need improvement. The results should be disclosed to appropriate stakeholders, in a form and manner selected by the governors.

The intent of the questions under each principle is to determine whether those in charge of the plan have considered the point formally. Thus, if the answer to a question is a "No", you should explain the approach adopted to meet the governance principle; and if it is "Yes", you should describe how it is implemented.

The questionnaire should be completed by the individual(s) with the best knowledge of the answer to each question, and approved by the highest level of pension plan governance authority (e.g., chair of the board of directors of the company, chair of the board of trustees, etc.).

Completed by:

Name	Title	Questions completed
Name	Title	Questions completed

Approved by:

Signature	Title

Principle 1: Mission	Yes	No	Describe
1. Does the pension plan have a mission statement?	O	O	
2. Has it been communicated to plan members?	O	O	

Principle 2: Fiduciary duty	Yes	No	Describe
1. Does the plan have articulated roles and responsibilities, and are there control mechanisms in place to protect the plan, the governors and administrators from conflicts of interest, lack of understanding and dishonesty?	O	O	

Principle 3: Responsibilities and accountabilities	Yes	No	Describe
1. Have the parties responsible for each of the following areas been clearly identified?			
a) Legislative compliance?[1]	O	O	
b) Plan funding?[2]	O	O	
c) Asset management?[2]	O	O	
d) Benefit administration?[2]	O	O	
e) Communication	O	O	
2. Are there clear written terms of references for each of the parties responsible for the functions listed under question #1?	O	O	
3. Are the names of governors and day-to-day administrators in charge disclosed to plan members?	O	O	

Principle 4: Supervision	Yes	No	Describe
1. Are there clear and objective measures of performance of the following areas?			
a) Legislative compliance?[1]	O	O	
b) Plan funding?[2]	O	O	
c) Asset management?[2]	O	O	
d) Benefit administration?[2]	O	O	
e) Communication?	O	O	
2. Is there a process in place to prepare regular reports to appropriate stakeholders and evaluate the attainment of performance in these areas?	O	O	

Principle 5: Governor's qualifications	Yes	No	Describe
1. Does the plan have criteria and a process for selecting the plan governors?	O	O	
2. Are the individuals responsible for the governance of the plan provided with training and orientation to fulfil their responsibilities?	O	O	

Principle 6: Governance self assessment	Yes	No	Describe
1. Are there processes and criteria in place to allow the individuals responsible for the governance of the plan to assess the effectiveness of the plan's governance and the individuals involved in it, on a regular basis?	O	O	

Footnotes:

1 Legislative compliance is not the sole responsibility of any single individual, but should be an objective of each governor, administrator, or other person or agent associated with the plan. It is a component of b), c), d) and e).

2 Refer to the following for examples:

Funding activities include:

- Establishing funding policies for the pension plan (e.g., targeted funding position such as fully-funded or the degree of over-funding).
- Approving the actuarial method and assumptions.
- Projecting the pension plan's cash flow.

Asset management activities include:

- Establishing investment policies and objectives (e.g., rate of return objectives, risk tolerance, asset mix, active vs passive management, pooled vs segregated, etc.).
- Selecting the custodian and the investment managers and rebalancing funds amongst the managers.
- Monitoring the performance of the investment managers, the custodian, the performance measurement service and the investment consultant.
- Monitoring compliance with the investment policies and contracts and mandates of external suppliers.

Benefit administration activities include:

- Establishing service standards.
- Enrolling members.
- Establishing and maintaining member records.
- Calculating and processing benefit payments.
- Calculating and reporting PAs, PSPAs and PARs.
- Creating and distributing member communication and education materials.
- Remitting contributions to the custodian.
- Monitoring accuracy and timeliness of major services to members against established performance objectives.