ACPM Brief to the Government of Ontario

Ministry of Finance

Phase II Reforms to the *Ontario Pension Benefits Act*

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ACPM/ACARR

The Association of Canadian Pension Management
L'Association canadienne des administrateurs de régimes de retraite

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FOREWORD

The Association of Canadian Pension Management (ACPM)

The Association of Canadian Pension Management (ACPM) is the informed voice of Canadian pension plan sponsors, administrators and their allied service providers. Established in 1976, the ACPM advocates for an effective and sustainable Canadian retirement income system through a non-profit organization supported by a growing membership and a team of volunteer experts. Our members are drawn from all aspects of the industry from one side of this country to the other. We represent over 300 pension plans consisting of more than 3 million plan members, with total assets under management in excess of $300 billion.

The ACPM promotes its vision for the development of a world leading retirement income system in Canada by championing the following Guiding Principles:

- Clarity in legislation, regulations and retirement income arrangements;
- Balanced consideration of other stakeholders' interests; and
- Excellence in governance and administration

Introduction

The ACPM is pleased to again provide our input to the Government of Ontario regarding the Government's announcement to proceed with the next phase of reforms to the Ontario *Pension Benefits Act* (the "PBA"). The ACPM is pleased with the efforts the Ontario government is taking to reform the pension system and address many of the issues that require attention. As third pillar pension providers, we look forward to lending our expertise to the Government of Canada and the provinces as you all move forward to meet the challenges that lie ahead for our retirement income system.

In this Brief you will find our perspective on certain of the proposed reforms to the PBA announced by the Ontario Government on August 24, 2010 (the "Announcement").

We are also attaching ACPM's 5-Point Plan; Improving Retirement Income Coverage in Canada which outlines our proposed solutions to expand and improve coverage in Canada.

1. CLARIFY SURPLUS ENTITLEMENT

The Announcement proposed to:

- "provide more legal certainty and a binding arbitration process for surplus distribution on plan wind up, while continuing to allow payment to an employer where there is entitlement <u>or</u> a surplus-sharing agreement;
- allow payment of surplus from an ongoing plan to an employer where there is entitlement or consent (i.e., two-thirds of members or bargaining agent, and retired members and other beneficiaries, as appropriate), provided the remaining surplus is no less than the greater of (i) 25 per cent of wind up liabilities and (ii) twice the current service cost plus 5 per cent of wind up liabilities; and
- ensure surplus rights are protected after asset transfers related to plan splits or mergers by requiring surplus-sharing agreements if plan terms differ."

While the references in subsections 79(3) and (3.1) of Bill 236 to subsection 79(3.2), and therefore also to the regulations under the PBA, raised an issue as to what conditions would be prescribed to permit surplus withdrawals, the better view is that surplus withdrawals could be made under the amended subsections 79(3) and (3.1) of the PBA on the basis of either entitlement or written agreement, subject to compliance with requirements prescribed under other sections of the PBA(for example, with respect to notices regarding surplus withdrawals). However, the Financial Services Commission of Ontario ("FSCO") announced through its "Pension Plan Administrator Questions Answered" on September 20th a different and quite extreme interpretation of these provisions:

> **Withdrawal of Surplus on Plan Wind Up**
>
> **Q: What is FSCO's position regarding applications for withdrawal of surplus on full or partial wind up now that some of the amendments made to section 79 of the *Pension Benefits Act* by Bill 236 have been proclaimed?**
>
> **A:** For applications for withdrawal of surplus on full or partial windup, made under s. 79(3) or (3.1), the employer must satisfy the requirements of clause (a) [employer entitlement] or clause (b) [surplus sharing agreement], and the requirements of s. 79(3.2). One of the requirements in s. 79(3.2) is that the applicant comply with all other requirements prescribed under other sections of the PBA in respect of the payment of surplus.
>
> If the employer is applying under clause (a) of s. 79(3) or (3.1), the Superintendent will approve the application if the employer demonstrates entitlement to surplus under the terms of the plan and all previous plan texts, has the agreement of the collective bargaining agent (or if there is no bargaining agent, the agreement of at least two-thirds of the members), and two-thirds of the former members and of other persons entitled to payments under the pension plan on the date of wind up and complies with all other prescribed requirements.
>
> If the employer is applying under clause (b) of s. 79(3) or (3.1), the employer is not required to demonstrate entitlement to surplus and the Superintendent will approve the application if all the members, former members and other persons entitled to payments under the pension plan consent to the application and the applicant complies with all other prescribed requirements.

As noted above, the Announcement states that in the Government's view the Bill 236 changes to the PBA provided that, on wind up, employer surplus withdrawal was permitted based on either (i) legal entitlement or (ii) a surplus sharing agreement. Therefore, the FSCO interpretation that 1) you must have entitlement <u>and</u> the surplus sharing agreement; or 2) the surplus sharing agreement must be at the <u>100%</u> level, does not seem in accordance with the government's intention and this matter should be clarified immediately. An amendment of Regulation 8(1)(b) should be made to state (i) in the case of subsections 79(3)(a) and 79(3.1)(a) that no consent threshold is applicable, and (ii) in the case of subsections 79(3)(b) and 79(3.1)(b) the consent level under the existing regulations.

In addition, Regulation 10 should be amended to deal with the requirements required for ongoing surplus withdrawals.

In addition, as noted above, the Announcement said that the government was proposing to "ensure surplus rights are protected after asset transfers related to plan splits or mergers by requiring surplus-sharing agreements if plan terms differ". The intention of this statement is not entirely clear. The legislation should specifically note that the protection is intended to protect surplus rights in plans splits and mergers only upon (and at the time of) a future termination of a merged pension plan. Therefore, the right to merge pension plans and cross-fund those plans after merger should be clearly stated not to be in any way restricted by these provisions. We also question whether adding additional restrictions on surplus withdrawals to plans that are merged or split is consistent with the recommendations of the Report of the Ontario Expert Commission on Pensions (the "Expert Report"), as it could have the effect of reducing opportunities for members to continue to have pension coverage following plan mergers and splits.

In addition, the proposal to provide a binding arbitration process for surplus distribution will have many procedural matters dealt with by regulation. However, the legislation should clearly address the basis for that arbitration. It should not be arbitration as to legal entitlement as that should be dealt with by the Courts. The legislation should identify the criteria to be considered by the arbitrator e.g., levels of contribution. It will also be important for the legislation to clearly describe the arbitration mechanism and provide that no arbitration should be required until a significant time has elapsed. Especially in non-union circumstances it may take more than two years after the approval of the applicable wind-up report to get the wind-up group organized, represented and in agreement.

2. CONTRIBUTION HOLIDAYS

The legislation should clearly state that contribution holidays are expressly permitted unless prohibited by plan documents, i.e. that the ability to take contribution holidays where the transfer ratio is at 105 or above is referring to the current plan text and not requiring an historical review of the plan documents. This is consistent with the Expert Report, see section 4.10.5. The threshold funding level of 105% together with the required disclosure should increase the security of benefits and while reference to current plan documents increases the efficiency by not requiring historical reviews and potentially time consuming and expensive litigation. Where an employee group wishes to restrict the right to contribution holidays that restriction should be included within the current plan documents. Therefore, contribution holidays should be expressly permitted unless prohibited by an applicable collective agreement or the current plan and funding document, without consideration of the historical plan document including the validity of any plan or funding document amendments.

3. PLAN EXPENSES

The Announcement states that reasonable expenses will be allowed to be paid from the pension fund "unless prohibited by the plan terms." Like contribution holidays, that restriction should only mean that restrictions included in the current plan text are relevant. Again, this is consistent with the Expert Report (see section 4.10.5). Accordingly, reasonable expenses should be expressly permitted to be paid from the fund unless prohibited by an applicable collective agreement or the current plan and funding document, without consideration of the historical plan document including the validity of any plan or funding document amendments.

4. INVESTMENT RULES

The Announcement states that the Ontario government continues to review the appropriateness of the 30% rule for pension investments. We would suggest that the 30% rule should be removed as unnecessary given the prudence standard in section 22 of the PBA. The ACPM has articulated a range of serious legal, policy and financial concerns with the 30% rule in successive submissions and remains firmly of the view that Ontario's pensions plans and capital markets would be better off without the rule.

5. JSPPS AND MEPPS

The Announcement contains proposals to exempt (i) existing JSPPs, and (ii) certain "target benefit" MEPPs, from solvency funding requirements.

We support the government's proposal to exempt JSPPs and target benefit MEPPs from solvency funding requirements, which promotes flexibility in plan funding and properly recognizes that funding rules should be modified to accommodate different plan designs. However, we recommend that the exemption be structured in a way that plans with similar risk profiles (and/or design features) to JSPPs and MEPPs would also be able to qualify for the exemption.

In particular, the solvency funding exemption that is being proposed for JSPPs and "target benefit" MEPPs should also be available to other types of plans that may not fall within these definitions, but which share similar characteristics to such plans (e.g., joint governance, risk sharing and/or the absence of PBGF coverage). It is important that the standard for extending exemptions from solvency funding requirements be flexible and capable of being extended to different types of plans, and not closed based on current definitions in the PBA. Also, the test for a plan to obtain solvency relief should be based on the underlying criteria articulated in the Expert Report, and not solely based on how a plan is labelled or defined for PBA purposes.

6. PENSION BENFITS GUARANTEE FUND (PBGF)

While we understand the government's desire to ensure the security of the Pension Benefits Guarantee Fund ("PBGF") we are concerned about the economic effect of these changes on plan sponsors, especially given that only Ontario employers are subject PBGF costs. We are also concerned about some of the assumptions in the Eckler Report regarding the funding of the PBGF and will provide a short comment on that Report.

7. SOLVENCY ACCOUNTS

We continue to believe that in addition to letters of credit, solvency accounts, which permit return of payments to plan sponsors, should be permitted under the PBA. While both letters of credit and solvency accounts provide funding flexibility and benefit security, given the challenge many plan sponsors find in obtaining letters of credit, solvency accounts are likely to be put to more common use. The ACPM will be making a detailed submission on this issue.

8. TARGET BENEFIT PLANS

We support the concept of offering target benefit plans as an alternative type of retirement plan,. We accept that joint governance is appropriate for target benefit plans. We believe that there are effective means to transition traditional defined benefit plans to target benefit plans, including providing the greater of (i) frozen salary projected benefits at the date of conversion, and (ii) the target benefits. We are currently in the process of preparing a further submission specifically addressing the subject of target benefit plans. We will forward this submission in the next short while.