Canadian Life
and Health Insurance
Association Inc.

Association canadienne
des compagnies d'assurances
de personnes inc.

June 23, 2014

Ms. Lynn Hemmings
Senior Chief, Payments
Financial Sector Policy Branch
Department of Finance Canada
140 O'Connor Street
Ottawa, Ontario K1A 0G5

Delivered by email: pensions@fin.gc.ca

Dear Ms. Hemmings:

Pension Innovation for Canadians: The Target Benefit Plan

I am writing on behalf of Canada's life and health insurance industry in respect of the captioned Consultation Paper, which was released on April 24, 2014.

Established in 1894, the Canadian Life and Health Insurance Association (CLHIA) is a voluntary non-profit association with member companies accounting for 99 per cent of Canada's life and health insurance business. CLHIA members provide services to approximately two-thirds of private pension plans in Canada, primarily in defined contribution plans, and a larger proportion of other workplace savings arrangements such as group RRSPs. Our members are also significant providers of "retail" savings plans, including locked-in retirement accounts (LIRAs) and Life Income Funds (LIFs) that hold amounts transferred from workplace pension plans.

Because of our industry's current focus on defined contribution pension plans, successor arrangements such as LIRAs and LIFs, and group RRSPs, we will confine our comments to topics where we believe our experience is relevant. The numbered headings below correspond to those contained in the Consultation Paper.

Impact on Existing Retirement Plans

While the Consultation Paper contemplates the possible transition of both defined benefit and defined contribution pension plans to target benefit plans, our view is that the latter transition is unlikely.

In general, employers seek to reduce difficult-to-manage variability in their financial obligations, and the potentially greater variability in an employer's pension contributions under a target benefit arrangement relative to those payable under a defined contribution plan would discourage employers from making such a substitution.

We note, however, that an employer may view a target benefit plan as providing an operational advantage in terms of attraction and retention of employees, and we would therefore not discount the possibility of the conversion of a defined contribution pension plan to a target benefit structure.

From a potential plan member's perspective, target benefit plans may be perceived as providing greater predictability of income benefits relative to defined contribution pension plans and individual savings plans such as RRSPs. We believe that this is not a fundamental characteristic of such plans, but merely reflects the limited use of guaranteed income products within the pension and RRSP market in recent years.

By pooling longevity experience, life annuities provide predictable, sustainable, retirement benefits at substantially lower cost than alternative strategies. And experience shows that where life annuities are coupled with consistent and robust contribution levels, defined contribution pension plans can provide guaranteed income benefits that compare favourably to those promised by defined benefit pension plans.

To the extent that current investment restrictions limit access to life annuities where the income payments are deferred more than one year from the date of purchase, greater flexibility may be warranted to facilitate periodic annuitization and to thereby limit individual plan members' exposure to the potentially adverse effects of interest rate-linked risk at retirement. ***We recommend that investment rules for all tax-assisted retirement arrangements permit the use of both deferred life annuities and immediate life annuities as, or as assets of, such plans.***

While CLHIA does not oppose adding target benefit plans to the available range of retirement plans available to federally-regulated employers and their employees, there should be no requirement to offer a target benefit arrangement, either where no workplace retirement arrangement currently exists or via conversion of any existing workplace retirement plan.

3. Objectives and Principles

The Consultation Paper's discussion of Pension Sustainability focuses on "an acceptable range of costs" and "effective risk management". Unstated is whose judgment should apply in assessing the acceptability and effectiveness of such measures. While we anticipate that the Office of the Superintendent of Financial Institutions may have some views regarding effective risk management, ***the acceptability of costs should be determined by the administrator and expert advisors within the governance model for the plan in question***, within the context of a competitive market for comparable services. In our view, acceptable costs should not be prescribed, since what is reasonable and acceptable should reflect the specific financial and demographic traits of the particular plan.

The Consultation Paper's discussion of Benefit Security contemplates that "the pension plan must include an integrated package of benefits, contributions, investments and funding policy developed and agreed upon by all relevant parties." The reality of developing and amending pension plans is that differing views may arise amongst various stakeholders, leading to possible reliance on mediation and, in some cases, arbitration. As is the case with collective labour agreements, some recognition and consideration of such dispute-resolution mechanisms within the broader plan governance framework and negotiation process may be warranted.

4.1 Administration and Governance

Conflicts of interest are an inherent risk in any commercial arrangement. In the context of pension plans, the key to addressing such conflicts effectively is not merely to minimize their occurrence, but to ***develop a transparent and accountable process to manage such conflicts*** as part of a robust governance regime. We would therefore suggest that the Consultation Paper's discussion of *Duty to Plan Parties* should be recast to acknowledge that <u>management</u> of conflicts of interest is paramount in importance to the <u>frequency</u> of their occurrence.

CLHIA believes that, in developing a governance structure for a particular pension plan, it is important to maintain flexibility appropriate to the characteristics of that plan. Imposing statutory or regulatory parameters, such as the number of participants in the plan's governance body, that do not reflect specific plan characteristics is, in our view, inappropriate.

With respect to the specific questions posed in the consultation paper:

1. Subject to the forgoing caveats, CLHIA generally supports the governance framework described.

2. CLHIA generally discourage prescriptive measures; in the context of the composition of a governance board, the focus should be on an appropriately diverse composition

to ensure that the impact of governance and administrative decisions on all groups of stakeholders are fairly represented.

3. CLHIA believes that, after seeking appropriate advice, the governance body should have the power to amend plan documents.

4. Given the potential for decision paralysis that can arise due to non-responsive plan members, imposing an absolute threshold for required levels of consent may be inappropriate. A simple majority of the quorum of stakeholders responding to a particular question - or a "super-majority" such as 2/3 of respondents - may be similarly insufficient. As an alternative, adopting a maximum percentage level of opposition to a proposed measure (rather than a threshold of explicit support), perhaps with separate measurements for respondents in each stakeholder class rather than on a total stakeholder basis, may be a more accountable means of balancing disparate interests and preventing stalemates in the decision making process.

5. The ability of labour organizations to represent both consenting members and those who choose, on a Rand-formula basis, not to participate in a labour organization is generally accepted. However, the ability of labour organizations to fairly represent the interests of retired members that may conflict with those of active members has sometimes been challenged. Consequently, it may be appropriate to permit separate representation within the governance framework for organizations representing retired workers, especially in the context of possible adjustment of pension contributions and benefits. While this separation of interests may be less significant in non-unionized environments, parallel rather than unified representation of active and former/retired plan members may be warranted in both unionized and non-unionized environments.

6. CLHIA lacks expertise in negotiated benefit arrangements in non-unionized environments and cannot appropriately respond to question 6.

4.7 Disclosure and Communications

Repetitive disclosure of unchanged information adds a significant cost to the operation of any pension plan. Recent increases in mailing costs compound this issue. As well, our experience is that consumer engagement is actually enhanced when information is made available, on demand, in a digital, rather than hard-copy, form, relative to the level of engagement observed when traditional printed materials are provided. By adopting electronic access, information is accessed and used when each consumer considers it to be relevant, rather than only at pre-determined, prescribed, times.

Consequently, we believe that disclosure models for target benefit pension plans, as well as for existing pension designs, should contemplate alternative access or delivery models, such as a website operated by or on behalf of the pension plan administrator. Ideally, ***electronic delivery should be adopted as the default communication for any*** new ***pension model***, supported by a "print on demand" capability for consumers who prefer "hard copy" documentation, and email "push" notices where member action is required.

With respect to the specific questions posed in the consultation paper:

1. CLHIA does not object to the proposed disclosure, assuming it can be provided in a cost-effective, electronically-based, manner.

4.8 Conversion of Pension Plans to Target Benefit Plans

We have commented above on the potential impact of the introduction of target benefit pension plans on existing plan designs, with a particular focus on the potential impact on defined contribution pension plans. With respect to the specific questions posed in the consultation paper:

3. While we believe such changes should be permitted, we believe that the demand to convert defined contribution pension plans to target benefit plans would be very limited, since this would incur additional risk for the sponsoring employer. In the longer term, conversion may provide some employer advantage, in terms of employee attraction and retention, but such benefits are not quantifiable at present.

4.9 Portability and Locking-In Rules

1. While accrued or commuted values of benefits are easily transferred between pension plans and successor instruments and this should be true for such benefits under target benefit plans, the ***portability of proprietary annuities that might be held by a pension plan is*** more ***difficult, since no secondary market currently exists for such instruments, and the current pricing of such products does not contemplate such a market.***
   Thus, while we encourage and support portability, we acknowledge certain limitations that are inherent in the use of long-term instruments that may be difficult to value, especially if the anticipated payment stream under such arrangements has a long but indeterminate term.

   Un-locking of long-term investments within pension plans poses similar challenges and incorporating such flexibility in underlying investments would result in higher overall cost. As a matter of public policy, CLHIA believes that ***pension plans are intended to protect retirement incomes, and unlocking to address current income needs is***

inherently inconsistent with that objective. At the same time, CLHIA acknowledges the challenges of balancing current and future income needs, and that compromises may be an appropriate public policy response.

At present, we see no target benefit plan-specific challenges to unlocking or portability of benefit entitlements.

Thank you for the opportunity to comment on this proposal. CLHIA members and I would be pleased to review our views with you and your colleagues as appropriate; as always, I can be contacted by telephone at 416-359-2021, or by email at rsanderson@clhia.ca, should further input or clarification be desired.

Yours sincerely,

(Original signed by)

Ron Sanderson
Director, Policyholder Taxation and Pensions