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SUBMISSION TO GOVERNMENT OF CANADA

Response to "Pension Innovation for Canadians: The Target Benefit Plan"

We are very pleased to provide feedback on the proposals of the Government in its consultation paper "Pension Innovation for Canadians: The Target Benefit Plan" released on April 24, 2014 (the "**Paper**").

We welcome the Government's announcement regarding target benefit plans ("**TBPs**"). In our view, enabling new and innovative plan designs is a critical part of promoting pension plan sustainability, adequacy and coverage. The Paper and this consultation are an important step toward providing both plan sponsors and plan members with greater flexibility and retirement savings options.

Our comments are made from the perspective of ensuring that TBPs are introduced in a way that puts them on a "level playing field" with other currently available pension options, specifically, traditional defined benefit ("**DB**") and defined contribution ("**DC**") pension plans, such that artificial barriers are not created which could impede TBP implementation. In particular, we comment on disincentives to the adoption of TBPs that may be present for certain employers if the TBP framework is more administratively cumbersome than necessary given the frameworks currently in place for DB and DC pension plans. We believe that a level playing field can be achieved, while at the same time meeting TBP policy objectives.

In our view, the following are the two biggest disincentives to the adoption and/or sustainability of new TBPs under the current Government proposal:

- Negotiation/consent requirements for the establishment and amendment of TBPs, particularly in a non-union context; and
- Governance requirements related to the functioning and representative make-up of the administrator of TBPs − in particular, the proposed requirement that the Board of Trustees be comprised of members, retirees and other beneficiaries.

As we set out more fully below neither requirement is necessary to establishing an equitable and transparent TBP framework.

We have approached our submission from a legal and regulatory perspective, as well as from the perspective of plan sponsors and administrators. For non-legal questions, we have drawn on our general experience and knowledge of the pension industry, but we have not attempted to address questions related to actuarial and economic matters.[1]

<u>Our Response and Recommendations</u>

We agree with the Paper's objectives – pension plan sustainability and benefit security – and its guiding principles – transparency and equity. We also wish to emphasize that flexibility will be key to a successful TBP framework. The TBP rules must allow flexibility in relation to plan design and governance in order to accommodate the different needs of different organizations and contexts (e.g., small employers versus larger employers, union versus non-union workplaces, new plans and conversions).

A. Administration & Governance

1. *Is this governance framework appropriate for federally-regulated private sector and Crown corporation pension plans wishing to convert to a target benefit plan?*

(a) Amendment Power

Under the *Pension Benefits Standards Act, 1985* ("**PBSA**"), the establishment of a pension plan and its amendment are the exclusive[2] purview of the sponsor of the plan and do not carry any obligation to consult or obtain the consent of plan members/beneficiaries or to act in their best interest in relation to such plan design decisions. This is in contrast to the administration of the plan once established, which must be carried out in the best interests of all plan beneficiaries free of unresolved material conflicts in the discharge of the administrator's fiduciary obligations. Plan design and amendment are subject only to the minimum standards requirements in the legislation and the provisions of the documents that constitute the plan. In contrast, the proposed federal structure for TBPs suggests that plan beneficiary consent be required as a prerequisite for the establishment of a new TBP, the conversion of a pre-existing pension plan to a TBP, and the amendment of a TBP once established. This effectively establishes a "joint sponsorship" structure in addition to a joint governance requirement on the administrative side (discussed below).

In our view, specifically mandating a consent/bargaining requirement for the establishment or amendment of a new TBP does not provide the necessary flexibility,

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[1] We understand that a separate consultation will be held on the tax rules applicable to TBPs, so we have not commented on tax issues here.

[2] In unionized workforce settings pension plans may be negotiated, but this is a matter of industrial relations outside the scope of the PBSA.

may be considered overly onerous by plan sponsors and will likely represent a significant impediment to the proliferation of TBPs in non-unionized workplaces.

We are also of the view that mandating a consent/bargaining requirement for the conversion of a pre-existing plan to a TBP could be unduly onerous. We note, for example, that in New Brunswick, the legislation providing for conversions to shared risk plans (a type of TBP), including the conversion of accrued benefits, does not require consent.[3] In our view, it is preferable to provide plan sponsors with alternatives – which *may* include a consent regime option – as we discuss further below.

In unionized workplaces, employment terms, such as the provision of a pension plan, must be negotiated and agreed upon in any event, pursuant to labour law and existing collective agreements. There is no reason in these circumstances for TBP legislation to impose additional consent/negotiation requirements to the establishment or amendment of a TBP, as long as any such amendment complies with the prescribed minimum standards. In New Brunswick, the majority of the plans that were converted had the full support of the applicable unions.

In non-unionized or partially unionized workplaces, the employer/employee relationship with respect to non-union employees is established at an individual contract level, not at a collective level, and there is no clear structure for negotiation on a collective basis. The requirement to seek collective member consent to the creation of a new pension plan and member input on its design features is completely foreign to the establishment or amendment of registered pension plans in the typical non-unionized workplace, and only currently exists in pension legislation with respect to employer surplus withdrawals – a very different context.

In order to give effect to any collective consent requirement tied to the establishment and design of TBPs, structures and processes allowing for employee representation would have to be created, which could pose a significant administrative burden and could create significant disincentives for the adoption of TBPs. Obtaining consent from deferred vested members and retirees can be even more problematic.

It is preferable, in our view, to protect plan beneficiary interests in relation to plan design and amendment by legislating minimum standards, which can only be contracted out of with appropriate levels of consent (as discussed below). With respect to plan conversions, where accrued benefits are at issue, we recommend that plan sponsors be given the option of *either* ensuring that the plan is fully funded to cover the accrued benefits as of the conversion date on a going concern basis *or* obtaining the consent of plan members. Where consent is required, we are of the view that such consent should be

[3] *Pension Benefits Act*, SNB 1987, c P-5.1, ss. 100.52(3.1)-(3.2).

obtained through an "opt out" regime – where no more than one-third of all plan members object.

(b) Board of Trustees

In our view, while in certain circumstances joint governance may be the collective preference of the stakeholders, the guiding principles of transparency and equity underlying the TBP regime can be achieved without *requiring* joint governance in all cases. Further, if joint governance is mandated, we are of the view that equal representation of employer and employee interests on a board of trustees or similar body is not necessary.

The joint governance requirement proposed in the Paper is significantly more onerous than the current requirements of the PBSA in relation to the administration of traditional DB and DC plans. As stated at the outset, to promote the "adoption" of TBPs, it is critical to ensure a level playing field among all plan design options unless there are compelling policy reasons otherwise.

TBPs have their own particular complexities, but are no more difficult to administer/govern than traditional DB and DC plans. A joint governance requirement may, in effect, make the entire regime a "non-starter" for many employers. Most federally-regulated organizations which could potentially establish, or convert to, TBPs currently provide single-employer pension plans, where the employer acts as both the plan administrator and sponsor. Moving to a joint governance model, which requires employee representation, may make TBPs unattractive to these types of organizations.

In our view, there are other approaches to ensuring that the TBP framework reflects the guiding principles of transparency and equity, which we discuss further below.

Other Joint Governance Experience

It is not clear that joint governance is necessarily preferable or achieves better results for members. For example, Québec has utilized a joint administration model (i.e., pension committees) for a number of years, and there is no evidence that such a model has resulted in such plans being better governed. Based on our experience, Québec pension committees often simply delegate most of their responsibilities back to the employer, which undermines the purpose of the legislated structure.

Moreover, in the unionized environment, joint governance has not been a panacea. There have been two notable instances where the governance practices of the boards of multi-employer pension plans ("**MEPPs**"), which have similar governance requirements as the proposed legislation, have been criticized (i.e., the cases involving the Canadian Commercial Workers Industry Pension Plan and the Participating Co-operatives of

Ontario Trusteed Revised Pension Plan).[4] In the case of the Participating Co-operatives of Ontario, the plan had to be wound up because a bad decision on the part of the board of trustees had made the plan unsustainable.

Current Law

Currently, the law effectively provides for a governance structure where duties and powers are divided between the sponsor and the administrator of a pension plan. The sponsor, often the employer, retains responsibility for plan design and funding, while the administrator is responsible for managing the plan and fund, including investment of plan assets and payment of benefits. The administrator – in contrast to the sponsor, who can act in its own interest – has a fiduciary duty to plan beneficiaries and is required to act in the best interests of plan beneficiaries and not in its own interest. Under the PBSA, the employer may act as both sponsor and administrator; however, when acting within the scope of its administrator authority, it must put the interests of plan beneficiaries as a whole first in the event of an unresolved material conflict between its role as administrator and employer. This "two hats" model is in place in all Canadian jurisdictions and has been recently favourably considered by the Supreme Court of Canada.[5]

In our view, there is nothing about the current provisions of the PBSA regarding the identity and duties of the administrator that is, in itself, incompatible with the administration of a TBP. That is, even if an employer were to act as administrator of a TBP without the involvement of plan members, it would be required by the legislation to act in the best interests of the beneficiaries as a whole when discharging its administrator duties. Moreover, the employer as administrator and fiduciary would be required to hold an even hand among beneficiaries and could not unduly prefer the interests of one group over another. Any member, retiree or other beneficiary representatives on a board of trustees would likewise be required to act in the best interests of all beneficiaries and not just in the interests of their own beneficiary group.

We also note that the governance structure described in the Paper appears to conflate the sponsor and administrator roles. For example, the Paper proposes that a Board of Trustees, which could include plan sponsors, would administer the plan, including being responsible for communications with members and the filing of required documents with the regulator, but could also delegate some functions, such as benefit calculations and plan member communications to a third party, including the plan sponsor. In addition, the

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4 See *R. v. Christophe et al.*, 2009 ONCJ 586 and *Re Participating Co-operatives of Ontario Trusteed Revised Pension Plan,* 2010 FST File No. P0275-2006. Also see *Deans v. Thachuk* 2005 ABCA 368.

5 See *Sun Indalex Finance, LLC* v. *United Steelworkers*, [2013] SCC 6.

Paper contemplates that the Board of Trustees itself have sponsor duties such as the power to recommend plan amendments. This complexity may be alleviated by following a more straight-forward governance structure already provided for in the PBSA.

The Paper also makes reference to including “other beneficiaries” on the Board of Trustees. It is not clear who would be included in this group, as “other beneficiaries” under a pension plan could include spouses or dependent children in receipt of a survivor pension, among others. Inclusion of such individuals in joint governance could be impractical as well as logistically difficult and is not currently required under other “joint governance” models, including on MEPP boards of trustees/pension committees established under s. 7(1) of the PBSA.

Finally, the Paper proposes that the Board of Trustees decide matters such as what the measures for deficit recovery and surplus utilization will be or what fund funding level triggers implementation of the funding deficit recovery plan. As noted below, we have suggested that the triggers for deficit recovery should be prescribed in the legislation. However, the other matters should be a matter of plan design. In our experience, it is preferable for plan terms to be as detailed as possible regarding issues involving a potential exercise of discretion. However, scenarios will certainly arise, both foreseen and unforeseen, where the exercise of discretion by the administrator will be necessary. Moreover, in certain circumstances, plan sponsors may want to build in more discretion for the administrator. We would suggest that the legislation allow for flexibility of plan design in these matters.

Transparency and Equity

Rather than mandating a joint governance structure, the Government could achieve the objectives of transparency and equity by providing for advisory committees to the administrator and/or independent experts to sit on an administrative body.

Allowing for input into the administrator’s decision-making process by affected beneficiary groups through a separate structure, such as a pension advisory committee, would, in practice, be helpful to ensuring that the administrator takes all relevant factors into account in making its decision and, as such, can show that it exercised its fiduciary duty appropriately. Moreover, it would allow beneficiaries to speak from the point of view of their own interest and make those fully known; whereas, if such beneficiaries were to be part of the Board of Trustees as contemplated, they would be obligated to set those interests aside and act in the interests of plan beneficiaries as a whole. As noted above, in the latter case, it may be difficult for members of the Board of Trustees who are also beneficiaries to show that they did not act in their own self-interest. The appeal of a pension advisory committee is that, while it gives the administrator access to the viewpoints of affected stakeholders, it does not potentially stall administrative decision making because competing interests are in conflict on the Board of Trustees.

Finally, we noted the Paper's suggestion that any administrative body could include an independent expert. In our view, appointing an independent expert to the TBP administrator body would be very valuable, particularly where a fully joint governance structure is adopted. An independent expert could inform administrator decision-making and help minimize deadlock and potentially expensive dispute resolution processes.

Summary:

a) **We would suggest that a consent regime be provided as an *option* (i.e., where the parties want to contract out of minimum standards), but not mandated with respect to all TBP amendments and/or the establishment of TBPs. With respect to plan conversions, where accrued benefits are at issue, the Government should consider giving plan sponsors the option of *either* ensuring that the plan is fully funded to cover the accrued benefits as of the conversion date on a going concern basis *or* obtaining consent of the plan members. Where consent is required, we would suggest that such consent be obtained through an "opt out" regime – where no more than one-third of all plan members object.**

b) **We would also recommend maintaining a similar governance regime for TBPs to that currently provided for under the PBSA. Options for achieving additional transparency and equity are advisory committees and independent experts.**

c) **If the proposed Board of Trustees structure is retained or if the parties choose to implement such a structure, we would suggest that "equal" representation of interests (i.e., equal number of employee/retiree representatives as employer representatives) need not be mandated (but could be agreed to by the parties) given that all members of the Board would be required to act in the best interests of all beneficiaries in any event.**

2. *Should the federal legislation or regulations be prescriptive regarding the composition of the governance body (e.g., proportion of plan members and retirees, presence of independent trustees)?*

As outlined above, we favour a non-prescriptive model for the composition of the governance body for TBPs to further the goal of putting TBPs on a level playing field with DB and DC pension plans. In particular, in a non-unionized context, the employer should have the flexibility to determine the composition of the governance body.

Where sponsors (whether employer or union) also act as administrators, the legislation could provide for a pension advisory committee to be established and permit the reasonable expenses of that committee, including the costs of retaining legal/actuarial experts to advise the committee, to be charged out of the plan fund. In addition, unions could be permitted to represent active members on the advisory committee. A potential model for such an advisory committee is currently available under PBSA s. 7.2, which provides for a pension council made up of employees and (optionally) retirees. For a more robust model of a pension advisory committee, refer to (new) s. 24 of the Ontario *Pension Benefits Act*.[6] While these models are not specifically tailored to the TBP context, they could be adapted, subject to the considerations set out above.

The legislation could also have permissive provisions allowing sponsors to establish a Board of Trustees structure for any given TBP, should that be desirable to the sponsor or the parties to a conversion. In that context, we also see the value in mandating the appointment of an independent (expert) trustee to the Board of Trustees, as discussed in response to Question A.1 above.

Summary: A non-prescriptive model for the composition of the governance body for TBPs is more likely to promote greater adoption of TBPs, and is preferred.

3. *Should the Board of Trustees have powers to amend plan documents?*

Currently, under the PBSA legislation, amendment of plan documents is a sponsor, not an administrator, function and does not require consent by plan members if the plan terms do not provide for it. The administrator is responsible for administering the amendment, filing it with the regulator, and providing notice of it, as may be required, among other things. We believe that this model, including the division of powers between sponsor and

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6 Once proclaimed in force, s. 24 will permit unions to represent members on the committee and provides that costs associated with the committee, as prescribed, may be payable out of the pension fund. It also includes the following plan administrator duties:

- distribute the notice of intent to establish an advisory committee and such other information as may be prescribed to the members and retired members;
- provide such other assistance as prescribed;
- meet with the committee as required by the regulations;
- provide such assistance to the committee as may be prescribed to help the committee carry out its purposes;
- give the committee or its representative such information as is under the administrator's control and is required by the committee or the representative for the purposes of the committee.

administrator, should be retained in the TBP context. In particular, the sponsor should retain the power to delegate certain amendments authority to the administrator, including a Board of Trustees, if any; however, in so doing the delegated authority should not necessarily lose its characterization as a sponsor function. Such delegation can be particularly desirable with respect to technical/compliance amendments. For example, the administrator should be able to amend the plan to ensure plan compliance with applicable legislation or to clarify an administrative procedure, as necessary and in such event, the amendment itself may be viewed as a fiduciary power to the extent it is compliance-based. However, we do not believe that the Board of Trustees should have powers to amend the plan beyond those delegated by the plan sponsor.

Summary: Similar to the status quo for DB and DC pension plans, plan sponsors should have the sole power to amend plans, subject to certain minimum standards set out in the legislation (as discussed below), and the authority to delegate such power, including to a Board of Trustees.

4. *What should be the plan member support level requirement for making substantial amendments to the plan text?*

In our view, consent requirements for plan amendments are not necessary except in certain limited cases. Imposing such requirements would be unduly restrictive and unwieldy, particularly if they are imposed across the board on all amendments, including technical/compliance amendments. That said, the Government could consider establishing minimum standards specifying certain fundamental amendments that require the consent of plan members (see examples below).

Under the current PBSA, plan amendments are prohibited in certain specific circumstances: namely, amendments that purport to reduce accrued benefits or the solvency ratio below a prescribed level are void (s. 10.1(2), PBSA), unless regulatory consent is obtained. This prohibition does not make sense for TBPs, since part of their purpose is to permit the reduction of accrued benefits as may be necessary to promote plan sustainability. As such, TBPs must be made exempt from s. 10.1(2), leaving them free to adjust benefits in response to affordability metrics without having to seek member approval. However, as noted above, a new provision prohibiting certain amendments to TBPs, except where adequate consent is demonstrated, could be set out in the legislation.

Such a provision could mimic the form of the current “void amendment” provision, with necessary modifications to account for the fact that accrued benefits may be adjusted under a TBP. To be consistent with the spirit of TBP core objectives, such a provision should also allow any prohibited amendment with consent. For example, the PBSA could provide that the following amendments require consent:

- changing the definition of base benefits (but not benefit reductions);

- changing the benefit reduction/restoration formula and/or priorities;
- increasing the parameters within which contributions may be increased.

Where consent is required, the legislation should recognize that obtaining positive consent to plan amendments can be very onerous and technically difficult, given that there is little incentive for plan members to respond in a timely fashion to requests for consent. Further, a balancing of sponsor/beneficiary interests is desirable if TBPs are to be an attractive option for sponsors considering establishing or converting to a TBP.

As such, we are of the view that an opt-out or objection system is preferable to a positive consent requirement. That is, we would recommend that the legislation provide that notice of the “consent” amendments be provided to affected beneficiaries prior to such amendments coming into force, and that such amendments shall come into force following a specified period after notice is given unless more than one-third of plan members object in writing to the regulator.

In the context of plan conversions to a TBP in unionized workplaces or the establishment of new TBPs pursuant to collective agreements, the parties may negotiate consent requirements to plan amendments to be reflected in the plan text. The latter is possible under the current legislative framework, which implicitly allows plan documents to impose constraints on the sponsor’s amending power in addition to those constraints contained in the legislation.

Summary: Should consent for an amendment be required, we would suggest that it only be applied to certain specified amendments (as outlined above) and evidenced through an “opt out” consent regime whereby plan amendments are passed where no more than one-third of the plan members object.

5. *Should there be different governance framework provisions applicable to federally-regulated pension plans in unionized and non-unionized environments?*

As we noted above, requiring a joint governance regime for TBPs may in effect make the entire regime less desirable for many employers – whether unionized or not. This disincentive may be particularly acute in organizations which are not unionized. Further, as we discussed above in our answer to Question A.1, we are not convinced of the benefits of joint governance in either union or non-union contexts. That said, we understand that the framework for the employee/employer relationship, and by extension, negotiation of employment terms, including benefit plans, is often different in unionized and non-unionized workplaces. The legislation could allow for different requirements in the two contexts, but without unduly constraining the parties in either type of workplace.

We would suggest that the legislation ensure, in a permissive rather than mandatory manner, that desirable governance structures exist for both unionized and non-unionized environments. For example, s. 7(1) of the PBSA currently provides that the administrator may be (1) in the case of a MEPP, a board of trustees or pension committee, and (2) in the case of a plan other than a MEPP, the employer, or a board of trustees or similar body if a plan is established under a collective agreement. The administrator should be permitted to be one of these entities in the TBP context as well and we would suggest that the list of possible administrator entities be broadened to permit boards of trustees or similar bodies in non-unionized contexts, as well as unionized ones, if they are deemed desirable in the particular circumstances.

Summary: We would suggest that the legislation be permissive rather than mandatory in respect of available governance structures for both union and non-union environments.

6. *What type of process could be used for negotiating provisions of the plan with employees in federally-regulated non-unionized environments?*

As noted above, we believe that the federal TBP legislation should not require employers in non-unionized workplaces to negotiate with employees to establish, or convert to, a TBP or (except in specified circumstances) to amend a TBP. In the alternative, should the Government determine that a consent regime is required in non-union workplaces, we are of the view that such consent should be evidenced by showing that no more than one-third of the plan members object. Where an amendment is prohibited absent consent, employers may choose to negotiate with employees to ensure their amendments go through without objection or they may choose to rely on the system of notice and objection to determine which amendments are permitted.

Summary: Should consent for an amendment be required, we would suggest that it apply only to significant amendments (as outlined above) and be evidenced through an "opt out" regime whereby plan amendments are permitted where no more than one-third of the plan members object.

B. Funding Policy

We understand that the funding rules that have been proposed for TBPs are intended to place a limit on employer liability and employee contributions, while ensuring that there is a high probability of delivering the target benefits and providing sufficient flexibility to adjust contributions and benefits to respond to changes in the plan's financial situation. Most of the questions in this section require input from those with actuarial expertise. However, we would suggest in response to the question "*How frequently should valuations be required?*" that the federal government require annual valuations.

In order for the TBP model to work and to minimize the impact of potential plan funding deficits, plan sponsors must have up-to-date information on the funded status of the plan so that they are ready to respond to any plan deficits in a timely fashion. Further, plan administrators will need to have a good understanding of the funded status of the plan for purposes of day-to-day administration (e.g., termination values may be adjusted by the funded ratio of the plan as of the most recent valuation). Annual valuations will help plan sponsors/administrators to meet these requirements.

We note, however, that it may not be necessary to require solvency valuations for information purposes, as currently proposed. While we will leave it to our actuarial colleagues to comment on this issue in detail, we are concerned that the use of a solvency valuation for information purposes, where funding on a solvency basis is not required, may be confusing to plan members. However, we would acknowledge that members do have an interest in knowing the funded position of their plan were it to be terminated and would encourage the Government to canvas the options in this regard.

Summary: Annual actuarial valuations should be required for TBPs.

C. Contributions

We understand that the proposed model would allow for increases and decreases in employee contributions and either fixed or variable employer contributions, subject to any agreement by the applicable parties.

1. *Is this approach to contributions for federally-regulated plan appropriate?*

An adjustment to the required contributions to a TBP may be a useful lever that could prevent benefit cuts. However, we would suggest that it be an optional matter of plan design, not a legislatively mandated requirement. In our view, it is very important that contribution changes not be the main or only lever available to plan sponsors when faced with funding deficits − sponsors must also be able to adjust benefit levels in response to funding issues.

2. *Should some of the specifics concerning contributions be determined by plan members or more fully prescribed in legislation or regulations?*

In general, the ability to adjust contributions should be an optional issue of plan design determined by the plan sponsor (and plan members where required), rather than mandated by the legislation or regulations. For example, in New Brunswick contributions are fixed, subject to narrow adjustments up to a prescribed amount in accordance with the plan's funding policy.[7] As we noted above, we are of the view that

[7] *Shared Risk Plans Regulation*, NB Reg 2012-75 [*Shared Risk Regulation*], ss. 9(1)-(3).

plan governance and design, including contribution levels, should largely be the purview of the plan sponsor. However, where significant changes to contribution levels are required, plan member consent may be required in accordance with the "opt out" regime described above in our answer to Question A.4.

Summary: We agree that plan sponsors should be permitted to include the ability to adjust TBP contribution levels (within a range set out in the legislation) in their plan design (in addition to the ability to adjust benefit levels) in response to funding issues.

D. Benefit Structure

The Paper proposes that TBPs provide a "targeted" rather than a defined or guaranteed benefit. The TBP framework would provide for two classes of benefits with a varying level of benefit protection:

- Base benefits could be reduced but would have a high level of protection and would only be reduced as a last resort.
- Ancillary benefits would have a lower level of protection and would be reduced before base benefits were reduced

1. *Is the approach of categorizing benefit in two classes appropriate?*

Yes, the proposed approach is appropriate, as it makes it clear – to plan sponsors, members, and other beneficiaries – which benefits receive the highest level of protection and which benefits are less secure. This approach is similar to New Brunswick's, which is also premised on two classes of benefits – base and ancillary – with different levels of protection.[8] Plan sponsors converting to TBP may further design their TBPs to fully protect pre-conversion benefits such that future adjustments are limited to post-conversion base and ancillary benefits. Flexibility will be important, as per our comments in response to Question D.2 below.

Summary: As proposed in the Paper, the legislation should adopt the approach of categorizing benefits into two classes – base and ancillary.

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8 Under the New Brunswick model, base benefits have a higher degree of protection. The design is such that at inception, there must be at least a 97.5% probability that base benefits will not be reduced over the next 20-year period.

2. *Should base and ancillary benefits be determined by pension plans or more fully prescribed in federal legislation or regulations?*

We would suggest that the legislation specify that, in the case of conversions, accrued benefits would constitute base benefits. Otherwise, base and ancillary benefits should not be prescribed by legislation. It is preferable to allow plan sponsors greater flexibility in this regard in order to incentivize plan sponsors considering a move to a TBP.

That being said, we recognize the plan members need a certain degree of certainty, and any changes to the definition of base benefits should require plan member consent as noted above in our response to Question A.4.

Summary: Apart from prescribing that in the case of conversions accrued benefits constitute base benefits, we are of the view that what constitutes base and ancillary benefits should not be prescribed by the legislation. We would suggest that amendments to what constitutes base benefits under any given pension plan should be subject to consent.

E. Funding Deficit Recovery Plan

1. *Should the deficit recovery measures and their prioritization be determined by plan members or more fully prescribed in federal legislation or regulations? If the latter, what measures should be prescribed and what should be the order of priority?*

The legislation should specify that the administrator must take corrective actions when the deficit recovery measures (as set out in the funding deficit recovery plan) are triggered. In terms of priorities, the legislation should provide that when addressing a plan deficit, base benefits (as identified in the plan documents) may only be reduced after reductions have been made to ancillary benefits. Such an approach is similar to New Brunswick, which requires that a funding deficit recovery plan be included as part of the funding policy, establishing an order of priority for corrective measures that the administrator must implement to address a plan deficit. We are of the view, however, that a more detailed list of priorities should be left to the plan sponsor (and plan members where required) to determine and to document in the funding deficit recovery plan.

The New Brunswick rules are prescriptive with regard to the timelines for implementation of funding deficit recovery measures and the minimum funding level to be attained through the measures. The federal Government may also want to prescribe timelines and the minimum funding level to be attained through such measures.

2. *Should deficit recovery measures be triggered as soon as PfAD starts to be depleted or the probability test is not met?*

While we will leave it to actuarial experts to comment on the exact requirements that should trigger the activation of deficit recovery measures, we are of the view that it would be helpful for the Government to prescribe such a trigger mechanism. For example, the New Brunswick shared risk regime provides for the trigger to be activated when the plan is less than 100% funded on an open group basis for *two consecutive* years.

Summary: We would suggest that the legislation prescribe a trigger for the funding deficit recovery plan, timelines and a minimum funding level to be attained through these measures. It should also specify that base benefits may only be reduced after reductions have been made to ancillary benefits, but leave remaining priorities to be determined by the plan sponsor (and plan members where required) and documented in the funding deficit recovery plan.

F. Funding Surplus Utilization Plan

1. *Should the surplus utilization measures and their prioritization be determined by plan members or more fully prescribed by legislation or regulations? If the latter, what measures should be prescribed and what should their order of priority be?*

We agree with the proposal that surplus ownership and surplus utilization should, for the most part, be a matter of plan design. However, legislation should provide that any surplus would first be used to offset any prior benefit reductions and should implement appropriate restrictions on surplus withdrawals while a plan is on-going. For example, the Government should prescribe a minimum funded level that should be attained before surplus withdrawal would be permissible.

By way of comparison, the New Brunswick rules provide that the first priority for any surplus must be the reversal of any prior base benefit reductions. In addition, the New Brunswick rules include a maximum amount of surplus that may be "spent" when the funding excess utilization plan is triggered.

We would recommend that these provisions could not be contracted out of in order to promote long term plan sustainability.

Summary: We would recommend that the legislation require any surplus first be used to offset any prior benefit reductions and make any surplus withdrawals while the plan is on-going subject to strict restrictions, including the maintenance of a funding "cushion" in the plan.

G. Disclosure and Communications

1. *What are your views on the proposed additional disclosure requirements?*

We are of the view that it is important to have additional disclosure to ensure that plan members fully understand the risks related to the benefits under a TBP and receive due notice of any benefit cuts/contribution adjustments.

The Government should consider prescribing member communications in respect of TBPs and providing that plan administrators may rely on a "safe harbor" (in relation to such communications) where they have communicated to members using the prescribed form or have included the prescribed content in their communications.

2. *What are your views on the timing, frequency and sequence for communicating these additional disclosure items?*

The Paper sets out a thorough list of communication requirements for TBPs. We note that the Government may wish to consider the extent to which differing circumstances should be taken into account when prescribing notice requirements. For example, those in receipt of payments from the plan may be in a position where they are less able to adapt quickly to significant changes in their payment stream.

Summary: The Paper sets out a through list of communications for TBPs. We would suggest that, where plan administrators have communicated to members using the prescribed forms/content, they should be able to rely on a "safe harbor" in relation to such communications.

H. Conversion of Pension Plans to Target Benefit Plans

1. *What are your views on how benefits are treated on conversion?*

We are of the view that the legislation should permit, but not require, accrued benefits to be converted to target benefits on conversion. In our view, a consent requirement need not be mandated for the conversion of a pre-existing plan to a TBP, but rather should be an *option* available to plan sponsors. Plan sponsors should be given the option of *either* ensuring that the plan is fully funded to cover the accrued benefits as of the conversion date on a going concern basis *or* obtaining consent of the plan members. An alternative to group consent is an individual opt out on conversion.

Where consent is required on a group basis, we are of the view that such consent should be obtained through an "opt out" regime – where no more than one-third of all plan members object.

2. *What views, if any, do you have on converting federally-regulated DC plans to TBPs?*

Conversion of DC plans to TBPs should be permitted. In general, converting a DC plan to a TBP would not raise many of the complexities associated with converting a DB plan to a TBP. For example, funding and accrued benefit issues would not come into play. In addition, such conversions would in the normal course only apply to DC account balances rather than pensions in pay. As such, we would suggest that such conversions could occur simply on the basis of applicable labour/employment law regarding changes to employment terms.

Summary: Plan sponsors converting from a DB plan should be given the option of *either* ensuring that the plan is fully funded to cover the accrued benefits as of the conversion date on a going concern basis *or* obtaining consent of the plan members. DC conversions should be permitted.

I. Plan Termination and Wind-up

1. *What are your views on applying solvency requirements in the case of plan termination within 5 years of conversion from a federally-regulated DB plan?*

We agree that the legislation should mandate the application of solvency funding requirements where TBPs are terminated (upon the request of the plan sponsor) within 5 years of conversion from a DB to TBP plan. Such a provision should be used to prevent conversions where the objective is avoidance of solvency funding requirements. New Brunswick also includes such an "anti-avoidance" rule in its shared risk regime.[9]

Summary: As you have proposed, if a TBP is terminated upon the request of a plan sponsor within five years of conversion from a DB plan, such conversion should be void and the PBSA requirements on DB plan termination (i.e., solvency funding) should apply.

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[9] Shared Risk Regulation, s. 17.