

GETTING OUR ACTS TOGETHER



Pension Reform in Alberta and British Columbia



Report
of the Joint Expert
Panel
on Pension
Standards

Executive Summary (Go to [complete Final Report](#))

The Joint Expert Panel on Pension Standards was appointed on October 19, 2007 by the Ministers of Finance of Alberta and British Columbia to conduct a full and independent public review of the pension standards legislation in the two provinces with a view to ensuring that the pension benefits standards contribute to making our provinces leaders in creating opportunities and choices for workers, investors and businesses. The *Pension Benefits Standards Act* (British Columbia) and the *Employment Pension Plans Act* (Alberta) (the Acts) set minimum standards for funding, investments, benefits and disclosure for occupational pension plans. Almost 1600 pension plans in the two provinces are subject to these standards. Public sector plans were excluded from the review.

The two Acts have not been thoroughly reviewed for two decades. During that time the occupational pension system has matured and become more complex, and pension plan participation has declined significantly in the private sector. Therefore, the Panel's key objective was to recommend changes that would strike a balance between encouraging the establishment and maintenance of workplace pension plans and giving plan members confidence in the security of their pension benefits.

The appointment of a joint Panel provided an opportunity to explore prospects for greater harmonization of pension standards between the provinces, responding to frequent calls for greater interprovincial harmonization.

The Panel has concluded that a fundamental reform of pension legislation is necessary to address these objectives. In crafting our recommendations we have attempted to balance the disparate views and interests of plan beneficiaries and employers, and the potentially contradictory goals of improved benefit security and higher participation. Consequently, we urge all readers of our report to view our recommendations as a package, which is intended to be taken as a whole.

Panel Recommendations

Following are our key recommendations:

Legislative framework

The governments should have as a stated public policy objective the encouragement of occupational pension plans as part of the “second pillar” of the retirement income system, complementing government programs and individual savings. This objective should not be included in pension standards legislation or in the Superintendent of Pensions' mandate; rather, the governments should jointly create the position of a “pension advocate”, who would be responsible for promoting pension coverage generally.

Pension Reform in Alberta and British Columbia

Standards should accommodate a wider variety of pension arrangements than were contemplated in the current statutes and should be tailored to the key characteristics of different types of pension plans – especially, to the risks associated with those different types of plans. At the same time, they should continue to promote transparency, accountability and benefit security. The legislative framework should be designed to be more principles-based, relying on principles where possible and rules where necessary. Strength and flexibility can best be achieved by articulating broad principles in the legislation, backed up where necessary by specific rules.

More principles-based legislation will necessitate equipping the regulator with the discretion and resources to enforce the principles effectively:

- the discretion to approve a variety of plan arrangements as long as they are consistent with the principles, and to issue guidelines specific to new plan arrangements
- the power to review and require changes to plan governance
- the power to impose administrative penalties for failure to provide key information that enables the superintendent to exercise his oversight role, and for failure to perform key administrative duties such as making contributions or providing benefit statements

The Panel recommends that, in order to promote and maintain harmonization, the two governments:

- adopt identical Acts in each province;
- establish a joint policy advisory council and a joint pension tribunal; and
- work toward the establishment of a joint pension regulator for the two provinces to administer the harmonized statutes.

In addition to their roles in maintaining harmonization:

- the joint pension tribunal would hear appeals of regulator decisions in both provinces to act as a “check and balance” to greater regulator discretion; and
- the joint policy advisory council would advise the ministers and the regulators in both provinces on policy and administrative issues. The council would be comprised of government policy advisors, private sector pension experts and the regulator(s).

We also urge the two governments to work toward national harmonization by championing the establishment of a national council of ministers responsible for pensions that would have a mandate to consider the viability of harmonized or uniform pension standards regulation across the country and a single national regulator.



Getting our Acts Together

Promoting confidence in the pension system

When pension plans fail to deliver on their promises, poor governance is often a root cause. In keeping with a more principles-based regulatory system, we recommend that:

- the widely-accepted “best practice” standards developed by Canada’s financial regulators for governance and for capital accumulation plans be adopted as principles in the legislation, and that the regulator be given discretion to assess plans accordingly and require remedial action if necessary;
- pension plans be required to have a governance policy, which includes a funding policy if the plan contains a target or DB provision, and to disclose it to members;
- current rules imposing quantitative limits on investments be repealed, making investments subject to the “prudent expert” standard, except that statutory limits on related party transactions should be retained;
- the statute clarify that fiduciaries in making investment decisions must make those decisions in the best financial interests of plan members and can take nonfinancial matters such as environmental, social and governance factors into account only as they affect the potential risk and return of the investment;
- individuals having statutory fiduciary responsibility be required to complete training programs at post-secondary institutions; and
- plan fiduciaries be provided a statutory defence if they can demonstrate that they have adhered to the governance guidelines and have acted in good faith, on an informed basis, in the interests of the beneficiaries, and in the absence of conflicts of interest.

Minimum funding standards should be tailored to the nature of the “pension deal”, the details of the pension promise that is reflected in the plan terms.

To overcome the impasse resulting from uncertainties about ownership of surplus in traditional DB plans, and its negative effects on the funding of these pension plans, the principles of the regulatory system should recognize that the promise that requires protection is the defined benefit rather than the contributions or surpluses that may arise. The Panel recommends:

- allowing pension plan sponsors to contribute funds in excess of those required on a going-concern basis to a separate fund (a “pension security fund”) from which amounts in excess of the calculated “wind-up basis”, after building in a reasonable margin, could be withdrawn by the sponsor;
- “ring-fencing” surplus ownership issues by allowing pension plan sponsors to “freeze” existing plans, preserving any existing entitlements to surplus and ensuring that accrued rights such as vesting continue, and to start new plans whose terms and conditions with respect to surplus entitlements would be clearly set out;



Pension Reform in Alberta and British Columbia

- continuing to allow irrevocable letters of credit issued by financial institutions to cover solvency deficiencies, as is currently allowed in both provinces;
- requiring surplus withdrawals or employer contribution holidays to be spread over five years with annual valuation updates to confirm that the plan continues to be in surplus to protect members from the volatility of pension valuations due to changes in economic factors such as interest and inflation rates;
- that the governments of British Columbia and Alberta encourage the federal government to review all of the income tax limits related to pension plans. The Panel recommends in particular that the limit on surplus that can be held in a pension plan be raised to 125 percent of liabilities; and
- that the governments encourage the federal government to extend the “super-priority” for unpaid pension contributions, contained in federal bankruptcy and insolvency legislation, to include due but unpaid special payments for solvency deficiencies and unfunded liabilities.

A new set of funding, disclosure and benefit rules is recommended for “specified contribution target benefit” plans, where the contributions are fixed by collective bargaining or a similar method but benefits are provided based on a formula:

- The plans’ funded status would be measured and any adjustments made on a going-concern basis. The plans would no longer have to prove that their assets would cover liabilities in the event of plan wind-up (“solvency basis”), but additional protections would replace the solvency funding rules:
 - There would be a requirement to hold a sufficient cushion to protect against unfavourable events, and a requirement to report the “settlement” status of the plan (whether the plan could pay out all benefits with existing assets) to the regulator and disclose it to members along with an explanation of the implications.
 - Benefit improvements would be restricted unless the plan has a sufficient funding cushion.

The Panel believes its recommendations for minimum funding rules would provide a solid foundation to promote benefit security in pension plans for the long term. However, recent events in the economy demonstrate that the governments should continue to use their power to provide temporary relief by easing funding standards in exceptional circumstances affecting all pension plans.

Individuals and the pension system

The Panel recommends that:

- the governments enhance and expand the financial literacy component of their high school curricula;



Getting our Acts Together

- the governments establish a clear mandate within government for enhancing financial literacy in the adult population; and
- the rules governing “unlocking” of pension monies that have been transferred out of a plan by a terminating employee be harmonized in the two provinces and that unlocking of 50 percent of pension funds should be allowed on a one-time basis if the owner is at least age 50, similar to Alberta’s current rule. The Panel recommends that plan sponsors be allowed to require a greater degree of “locking in” as a term of their own plan.

Improving pension coverage

While a new generation of pension standards legislation is a necessary basis for a solid occupational pension system in the future, in our view it is not sufficient. Just over 20 percent of private sector workers in the two provinces are enrolled in pension plans. Employers often cite expense, administrative burden and risk as reasons why they do not offer pension plans. We advocate that the governments of British Columbia and Alberta create a new pension plan, to be operated as a non-profit entity at arm’s length from government but regulated under the pension standards legislation. The Panel recommends that a Steering Committee be established, comprised of experts in all facets of pension plans to determine the feasibility of establishing such a plan, obtain public input and recommend the plan design

The following are the Panel’s recommendations for the key characteristics of such a plan:

- The plan would be available to any employer, employee or self-employed person at a reasonable cost, enabling them to take advantage of the economies of scale afforded by pooling pension risks and assets as well as access to investment expertise and products not currently available to small pension plans and individual investors.
- Administration and investment management should be competitively tendered. To be successful, total expense ratios for this type of plan, including investment management and administration expenses, should not be greater than 0.5 per cent of assets under management.
- The plan would be a simple defined contribution plan, and enrolment would be automatic for employers and employees, who could opt out if they did not wish to participate. Self-employed people could participate by opting in.
- Employees and employers would not have any discretion with respect to the investment of plan assets, which would be invested subject to the policy direction of the board of governors.
- Provision of annuities from within the plan should be considered if the plan becomes large enough.



Pension Reform in Alberta and British Columbia

- Although some start-up costs would likely have to be financed by the governments, the governments would have no ongoing costs or liabilities. The plan would be subject to the same regulation as any other registered pension plan in the two provinces.

