

Submission to the Ontario Expert Commission  
on Pensions

by the National Automobile, Aerospace,  
Transportation and General Workers Union of  
Canada (CAW-TCA)

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## **CAW Submission to the Ontario Expert Commission on Pensions**

On behalf of the 260,000 members in Canada, and more particularly the 159,000 members in Ontario, the Canadian Auto Workers (CAW) appreciates the opportunity to appear before this Commission.

The CAW represents workers in a wide variety of workplaces and sectors, including the automobile industry; aerospace; mining and smelting; air, rail, water and road transportation; health care; hospitality and gaming; universities and colleges; fisheries; services; and general manufacturing. Our members participate in an equally wide variety of pension plans, including Defined Benefit (DB) and Defined Contribution (DC) plans, as well as other money purchase arrangements. While the vast majority of our members are covered by a workplace pension plan, some have no coverage. In part this has resulted from mergers with other smaller unions which have not had the resources to adequately address pension issues.

Our union also represents tens of thousands of retired workers and surviving spouses, who live in communities across Canada. Our retired members are organized into retired workers chapters, and many remain active in the union through their local unions.

The CAW's perspective on pension issues is based on our experience with and commitment to the workers we represent, both at the workplace and in retirement. The real, practical world of labour relations, which at times provides both opportunities and constraints, has shaped our view on pension issues. At the same time we acknowledge that many workers in Ontario are both without a union and without a workplace pension. The observations and recommendations we make below are guided by the principle that secure and adequate incomes in retirement are rights to which all workers are entitled.

We are encouraged that the focus of the Commission's work is centered on "the importance of maintaining and encouraging the system of defined benefit pension plans in Ontario". In announcing this initiative, the Minister of Finance stated that the Commission was appointed in order "to examine the legislation that governs the funding of defined benefit plans in Ontario, the rules relating to pension deficits and surpluses and other issues relating to the security, viability and sustainability of the pension system in Ontario." The CAW is pleased to share its views on many of these critical issues.

## **A Broader Perspective**

While the terms of reference which guide the Commission include the issues of funding, surplus rights, wind ups, and the Guarantee Fund, there is virtually no reference made to the central issue of the adequacy of retirement income. After all, we should be concerned about pensions precisely because of our concern that a pension system must provide our citizens with an adequate and secure income in retirement. In that regard, the CAW-Canada is disappointed that the mandate of the Commission was not set more broadly. The work of the Commission has the potential for influencing and setting the framework for a wide-ranging discussion on retirement income across Canada.

In Canada and Ontario, income security in retirement is often described as a three-tiered system: the responsibility for retirement income is shared among government, employers, and individuals. In other words, there is a recognized role played by public plans such as Old Age Security (OAS) and the Canada and Quebec Pension Plans (CPP/QPP), employer sponsored Defined Benefit (DB) and Defined Contribution (DC) plans as well as the savings vehicles chosen by individuals. The relationship and interplay between these tiers is complex, but any serious examination of the “pension system” in Ontario must take this connection into account.

While we are mindful of the jurisdictional limits of any provincial review of “pension systems”, we respectfully suggest that the Commission seriously consider taking a broader perspective. In February, 2007, the Commission published a Discussion Paper which raised the many serious pension related issues confronting the Commission. These included declining coverage rates, the shift from DB to DC plans (and the attendant shift of risk to workers), the changing pattern of employment, the particular needs of women and immigrants, and of course the related issues of funding and benefit security. In this context, it is abundantly clear to us that most of these concerns could best be addressed by a greater reliance on those public plans which have been proven to be superior in almost all respects.

In addition to providing virtually complete coverage of the paid work force, allowing for full portability for earned pensions, public plans such as the CPP/QPP plans can deal with many variables such as the risk of inflation, the risk of layoff and/or time out of the labour force, the risk of stock market and interest rate volatility, the flexibility to provide for early retirement and the ability to deal with disability. In addition these plans are characterized by low

administration fees, and stable and predictable contribution levels. Perhaps the most important attribute of the CPP/QPP and OAS is the benefit security which underlies these public plans.

The CAW urges the Commission to recommend that the Ontario government actively pursue discussions with the Federal and other Provincial governments to seek expansion and improvements in our current public plans. Greater reliance on those plans will help to not only reduce dependence on private plans, but will also help to stabilize their funding obligations.

### **Workplace Pension Reform**

Canada's public pension system has for the most part delivered the goods. It has provided most paid workers with guaranteed, indexed benefits at extremely low administrative cost, and it has been a prime constituent in reducing poverty amongst seniors. However, for many workers, this public source of retirement income is not adequate, and we therefore understand the need to improve and stabilize workplace pension plans. In particular, workplace pensions often make the difference between mere basic adequacy and survival and a comfortable retirement. And workplace pensions continue to be indispensable as a source of income for retirements prior to age 65.

Overall pension coverage in Canada has been declining for some time. Between 1977 and 2003, the percentage of paid workers covered by a registered pension plan went from 46.2% to 39.3%. In Ontario, coverage went from 47.9% to 38.5%.<sup>1</sup>

Private sector pension coverage is declining even more rapidly. Whereas in 2003 only 28 percent of private sector employees even had any sort of pension plan (down from 34 percent in 1991), by 2005 the situation has deteriorated. According to Statistics Canada, the coverage rate in the private sector has declined to 25.9%.<sup>2</sup> Almost three-quarters of Canadians in the private sector have no employment based pension. This report also confirms that "the largest decline (*in registered pension plans*) occurred in Ontario, where membership fell by 5,020 members to just under 2.2 million. The decline occurred mainly among men, and was concentrated in the manufacturing and trade industries."<sup>3</sup>

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<sup>1</sup> Patricia Schembari, "Employer-sponsored pension plans over the last 30 years", Canada's Retirement income Programs, Statistics Canada Cat. No. 74-507-XCB

<sup>2</sup> Statistics Canada, The Daily, June 21, 2007

<sup>3</sup> Ibid.

For the period between 2002 and 2006, while the number of DC plans in Ontario hardly increased, membership increased by 16.6%, while DB members increased by some 7.6%.<sup>4</sup> These percentage increases mask the absolute numbers – while DC membership increased by 48,643, DB membership in Ontario increased by 121,410. Of the 121,410 increase, fully 101,747 or 84% was represented by the growth in female participation in DB plans.<sup>5</sup> DB plans and membership continue to be the most significant component within registered plans in Ontario.

Declining coverage is due to a variety of factors, including declining union membership – workers are far more likely to be covered by a DB plan if they are union members. It is also a result of the shifting pattern of employment – employment in the service, hospitality, retail and finance sectors is typically not associated with pension coverage. We would suggest that consideration should be given to more flexible arrangements for the setting up of multi-employer pension plans (MEPPS). This has the potential to provide relatively low cost pension vehicles for small and medium sized workplaces which would otherwise not be able to offer any form of DB coverage on their own.

### **Defined Benefit Plans**

Although the Discussion Paper briefly notes some of the characteristics of DB plans, and contrasts them with those of DC plans, we believe it is important to more clearly emphasize the differences and discuss why defined benefit plans provide a vastly superior method for the provision of retirement income for workers. We feel compelled to make these points particularly because of the extreme pressures faced by workers and their unions – pressures from many employers who are attacking negotiated defined benefit plans. These attacks take the form of proposals to either freeze or eliminate current plans, or convert them into DC vehicles.

At one level, the methods for the provision of pension benefits can be simply stated. All plans, whether they are DB or DC, rely on the same principles:

Money is set aside in a special fund prior to retirement to provide for income after retirement;

In both cases, the money is tax exempt when set aside, and taxable when paid out;

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<sup>4</sup> Statistics Canada, CANSIM , 280-0009

<sup>5</sup> Ibid.

In both cases, the money set aside generates interest and earnings;

In both cases, the money in the fund must be converted into a regular retirement income

While all types of pension plans are built upon some basic principles, there are, however, significant differences with respect to the flexibility of overall arrangements, and the degree of risk for workers as compared to employers.

By flexibility we mean the capacity of a pension plan to provide various features and options, in addition to the straightforward objective of a retirement income for the worker involved. Amongst the more important of these features and options are: subsidized early retirement; bridge or "supplemental" benefits; credit for past service; special disability benefits; spousal benefits; post retirement indexing; and, early retirement windows or special retirements. What enables DB plans to provide this kind of benefit is that they are by their very nature a collective instrument. In most DC type plans these sorts of arrangements are either impossible or extremely difficult to fashion, since the only source of funds in DC plans is the individual's own account.

The second major concern which has to be addressed is the question of risk. Any pension plan involves certain elements of risk which can jeopardize the security of pension benefits. Under DC plans, risk is borne to a much greater extent by workers rather than employers.

The risk in these sorts of plans is two-fold. First there is investment risk. If the investment performance of the DC account has been relatively poor, this will mean that the individual account will be lower, and obviously, the subsequent pension will be lower than it would otherwise have been.

Secondly, we refer to the annuity or interest rate risk. In DC plans individual workers are at the mercy of the long-term interest rate environment at the time they retire. If long-term interest rates are low at such time, the purchase of an annuity becomes very expensive. Long-term rates vary constantly and significantly and can translate into significant differences in pension income for a given amount annuitized at different times.

In all DB plans, however, the employer is ultimately responsible to pay any amounts which are required to fund the promised benefits. In DB plans,

therefore, to a significant degree, the risk of inadequate investment returns, low interest rates, higher than expected retirement rates, etc. are borne by the employer. Employers are better able to absorb such risks since they have the capacity to collectively share these risks across workers of different ages, which means that the volatility of investments and interest rates will be smoothed out over time.

### **Funding and Surplus**

The funding difficulties of many DB plans has been extensively reported and commented upon. The main factors giving rise to these difficulties have been the significant collapse of equity markets combined with perhaps an even more important decline in the long term real interest rates which have been used to value pension liabilities. In addition, changes to the basis for calculating commuted values and the adoption of more relevant mortality assumptions have also played a role in increasing financial pressures on pension administrators. As an aside, it would appear that many of these pressures have also had a severe impact on DC plans – their reliance on equity markets and the need to convert pension balances into annuities at a time when annuity rates are at historically low levels have combined to create similar problems in the DC world.

We note that while many DB plans are adequately funded on a going concern basis, the requirements for solvency funding – which basically assumes plan wind ups – have undoubtedly created difficult circumstances for many employers. Suggestions for dealing with solvency funding issues tend to focus on questions about the appropriate amortization period for paying off unfunded liabilities or about the need to establish certain kinds of contingency reserves or even adopting different asset allocation strategies. These suggestions are invariably framed by a concern that employer contributions are somehow limited because of the uncertain ownership of resulting surpluses.

Funding issues are frequently coupled with concerns about surplus. Employers often argue that they should not be subjected to stronger funding requirements because in doing so, they may be creating surpluses that they will not be able to access or utilize.

The Discussion Paper notes that the argument made by some that “since employers must make good deficiencies suffered in bad times, it is only fair that they should be able to recoup their fortunes if a fund produces a surplus in good times.” This assertion is widely known as the ‘asymmetric risk argument’.

As we have noted elsewhere, “the CAW-Canada does not accept the “asymmetrical risk” argument for employers funding defined benefit pension plans. From a union perspective, it is hard to see the asymmetry when employers have been enjoying the benefits of pension surpluses over the past 20 years. In fact, in the 1980s employers lobbied against an expanded public pension system and insisted on the right to maintain workplace pension plans. The workplace plans had surplus funds, and employers took full advantage of using surplus to fund contributions.”<sup>6</sup>

While there is a superficial logic to the asymmetrical risk argument, it is one which ignores the dynamic process of collective bargaining in unionized workplaces and the usually unbalanced power relationship in non-union workplaces. Employers do not simply accept the requirement to fund pension deficits. A typical bargaining session finds employers forcefully advancing their case, asserting their inability to continue to fund these deficits and at the same time provide other improvements. Indeed, employers often take positions such as freezing or abolishing their current defined benefit plan. In other words, employers try, and many times succeed, in shifting the risk by forcing inferior results either directly or in other parts of the ‘compensation package’. There is reason to believe that these outcomes in non-union workplaces are even more pronounced.

At least some in the pension industry recognize the limited applicability of the asymmetric risk argument. In a backgrounder published by the C.D. Howe Institute, Keith Ambachtsheer points out;

“In DB plans ... there is a fiction that all risk-bearing is done by the employer, and that employees are guaranteed a pre-defined pension on retirement. In practice, this is not how things usually work. It is true that the employer is on the hook to make additional contributions when calculated plan liabilities exceed assets. However, plan participants are risk bearers too.

For example, the employer may go broke or simply terminate the plan. Employee pension contributions may also rise. Even if not directly, higher employer pension contributions could lead to lower current

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<sup>6</sup> CAW –Canada’s Submission in Response to Finance Canada’s Regulatory Framework for Federally regulated Defined Benefit Pension Plans Consultation (2005)

compensation for employees... A significant portion of the inflation risk embedded in DB plans is typically borne by plan participants, and not the employer...in short, despite the risk-free fiction, DB plans are virtually always risk-sharing arrangements.”<sup>7</sup>

A recent tabulation which the CAW requested from Statistics Canada revealed that for 2006 about 79% of the members of Canadian DB plans are required to make contributions. Many of these plans are collectively bargained wherein member contributions are subject to the bargaining process and hence subject to the “risks” associated with pension deficits.<sup>8</sup>

The proponents of the ‘asymmetrical risk’ argument usually make scant reference to the well-known and pervasive practice of employers taking contribution holidays in at least the two decades of the 1980s and 1990s. It is apparent to us that many employers were able to excessively use contribution holidays to offset their required contributions and as a result have ended up with plans in significantly under-funded positions at a later time. It is somewhat disingenuous for employers to now be arguing that there is some sort of unfairness when they are required to fund deficits after having utilized previous surpluses through the use of contribution holidays. Accordingly we think it important for the Commission to undertake the necessary research which would analyze the interconnectedness of the recent history of surpluses, contribution holidays and funding deficits in Ontario.

We remain sceptical that providing greater access to surplus will induce employers to provide improved funding or improve DB coverage. Funding of pension plans is only one of many competing priorities for most employers and access to an unknown and uncertain surplus will not be a determining factor.

We do, however, understand that there can often be a direct contradiction between the requirements for stronger funding and the resultant impact on benefit security on the one hand, and on the other the potential for overly burdensome pension financing at the expense of an employer’s capacity for funding other business expenditures.

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<sup>7</sup> Keith Ambachtsheer, “Cleaning Up The Pensions Mess: Why it will take more than money”, C.D. Howe Institute, Backgrounder No. 78, February, 2004

<sup>8</sup> Special Tabulation, "Pensions in Canada Survey" of Statistics Canada

We also recognize that some plan sponsors face severe funding obligations; in part because of external factors and we support measures for funding relief which would not jeopardize the security of the pension benefits.

We also think that it is extremely important to note the temporary nature of pension funding shortfalls. The market conditions which led to pension shortfalls for some defined benefit plans are improving. Even some plan sponsors who demand immediate funding relief anticipate large surpluses accruing in the next few years.

Recent observations by industry observers tend to support this view. For example, Dominion Bond Rating Services (DBRS) in a recent study of DB plans in North America has concluded that "...the health of defined benefit plans appears to be headed in the right direction."<sup>9</sup>

A recent press release by a leading actuarial and consulting firm has confirmed the general observations made above. "Pension funded ratios have reached their highest levels in five years as conditions for Canadian pension plans steadily improve."<sup>10</sup> The retirement practice director of this company's Canadian operations also concludes that

"Now, plan sponsors not only expect next year's budgeted pension expenditures to be lower, but it looks likely that the markets will help the cash side of their business operations. We are now moving back towards a world of pension surpluses."<sup>11</sup>

Nevertheless the CAW remains open to policies and regulations which can provide flexibility for pension funding, but we can entertain such changes only if they are coupled with policies that provide for greater benefit security. For example, proposals to extend solvency amortization periods on their own do not necessarily represent any improvement, other than providing financial relief for employers. In fact, they add to the possibility of reduced benefit security should the enterprise fail before all payments are made. Unless such funding proposals are coupled with direct measures to provide benefit security, they will not gain our support.

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<sup>9</sup> DBRS, Industry Study, "Pension Plans: The Myth of a Pension Problem", august, 2007, p.8

<sup>10</sup> Ibid

<sup>11</sup> Watson Wyatt Canada, "2007 Continues to Look Good for Pensions", Press release, July 9, 2007

## **Pension Insurance**

While Ontario has the only form of pension insurance in any Canadian jurisdiction, the Pension Benefits Guarantee Fund (PBGF), it is woefully inadequate. The amount of insurance which it provides and the resources available to the Fund do not provide the benefit security that pension plan members should expect. The \$1,000 limit on coverage has not changed in over 27 years and the financing provisions are insufficient. The PBGF either has to be improved, or some other form of pension insurance must be implemented. While there are some potential difficulties in pension insurance schemes, including those of adverse selection and moral hazard, we must collectively find a way to provide protection for retirement income. It is difficult to see how we can agree to relaxed funding requirements or entertain any proposals for more access to surplus for employers, unless the central issue of benefit security is directly addressed.

## **The PBA and Federal Law: Creation of Economic Insecurity**

Workers invest their knowledge, time, skills and labour in exchange for a promise of payment of current and future wages and benefits. Pension plan benefits are among the most significant deferred benefits that accrue to workers. Such benefits provide economic security and stability to workers during their retirement. When a company becomes insolvent the consequence for workers is frequently devastating; not only are workers faced with the hardship of unemployment and immediate loss of income, they may also suffer future losses as a result of unfunded pension liabilities and the inability of the pension regulator to make a claim as a secured creditor.

Pension legislation has, as its primary purpose, the protection of benefits for plan members, but the effect of the Canadian constitutional framework undermines this goal. Accepted constitutional doctrines provide that where there is a conflict between two validly enacted provincial and federal laws, covering the same subject matter, the federal laws will prevail and the provincial legislative efforts must fail. In the context of bankruptcy, the interplay between provincial pension benefits legislation and the federal Bankruptcy and Insolvency Act, (the "BIA") R.S.C., 1985, c. B-3, leaves workers economically vulnerable at retirement. When a company that sponsors a pension plan becomes insolvent, while contributions to the pension plan are in arrears, workers who have invested their labour, skills, talent and time into that company are stripped of any measure of protection in respect of their future pension benefits. Because the relevant

provincial pension regulator and/or a plan administrator is only permitted to make an unsecured claim against the property of the bankrupt company, unfunded pension liabilities are rarely recovered.

A concerted and cooperative effort is required to create a legislative regime which will protect the pension benefits of workers. The primary way to safeguard vulnerable workers in the event of bankruptcy is by ranking underfunded pension funds higher on the list of priorities in bankruptcy situations and positioning them in the secured claims category. This will ensure that pension plans are ultimately better funded and the earned benefits of workers are not compromised by bankruptcy. When workplaces close their doors workers bear the immediate burden of economic insecurity, they should not be subject to further loss in the form of cutbacks to their pension benefits. It is long past time that the labour of workers is recognized as a secured asset deserving of the same protection as that which is provided to companies' secured creditors. Just as a bank loans money to a company, a worker loans the value of his or her labour to the company in exchange for a promise of future recovery in the form of pension benefits. There is no justification for treating a worker's loan of the value of his or her labour any differently than the dollars provided by financial institutions. Such a change would represent sound economic and social policy by meeting the dual goals of providing income security to our society's older members and by placing the responsibility of paying for such benefits squarely on the shoulders of the companies that benefited from the provision of labour.

### **Provision of Windup Reports to the Bargaining Agent**

Representing workers in workplaces which are closing their doors or where workers are facing mass layoffs is rife with difficulty. At such times of turmoil, unionized workers turn to their union for assistance and support. Unions, who have been democratically selected by the employees to represent their employment interests, are too frequently frozen out of the processes by which decisions affecting the futures of their members are made. Recently, there has been an unwelcome trend of failing to disclose certain parts of reports in respect of partial and full windup of pension plans to the bargaining agent of affected workers. Privacy interests have been cited as the basis for refusing to disclose individual member information contained in the windup reports to the bargaining agent. Information such as age, gender, service and name is vital to ensuring the accuracy of the data, and by extension, ensuring that plan members' rights are fully protected in these circumstances. Despite the reliance on privacy legislation

by the Superintendent of Pensions, there is no logical or legal rationale for barring the bargaining agent from accessing information in the windup reports.

In the context of labour relations, it has consistently been found that to fulfill its statutory obligations a union must be able to communicate with the workers it represents and that an employer's refusal to furnish the information needed to communicate with those employees, may constitute interference in the union's representation of bargaining unit members (see for example, *Ottawa-Carleton District School Board*, [2001] O.L.R.D. No. 4575, *Alcohol and Gaming Commission of Ontario*, [2002] O.L.R.D. No. 120, *York University Staff Association v. York University*, 2007 CanLII 22560 (OLRB) — 2007-06-04). These decisions underline a basic principle: there is nothing improper or unwarranted in providing unions with information related to legitimate labour relations interests. Information in respect of a wind-up of a pension plan, affecting members of a bargaining unit, is the exact kind of information to which a union must be entitled. As unions are not commercial entities the privacy protections found in the preeminent privacy statute in Canada, "Protection of Information and Personal Disclosure Act" ("PIPEDA") do not apply.

### **Timeliness of Orders and Section 69 of the PBA**

Discipline needs to be introduced into the pension benefits system where section 69 is engaged. Under section 69 of the *Pension Benefits Act*, R.S.O., the Superintendent may order the windup, in whole or in part, of a pension plan where certain criteria are met. Sections 70-4 outline the process of wind-up. There are currently no legislative restrictions which govern the timely provision of a final windup report. While the availability of resources may be frequently, and fairly, pointed to as justification for a lack of rapid action in providing such reports, the delay compounds the negative effect on workers. It is not uncommon for the wind up process to take many months and in some cases several years. Workers who have lost their jobs and income, and often their health care and other benefits, should not be subjected to unacceptable delays in receiving their retirement income. Regulations must set firm deadlines by which the Superintendent will be required to provide the final windup report and which make the Superintendent answerable for a failure to meet these time limits.

## **Plan Mergers and Employee Contributions**

Employers sometimes seek to merge two pension plans and use the surplus of one of the plans to fund the obligations of the other. When the pension plan in a surplus situation is a defined benefit contributory plan, comprised largely of the contributions made by workers, which are topped off by the employer, unique issues arise. Equity and fairness would seem to require that workers, as the parties who made the contributions to the fund, be entitled to the benefits of those contributions. Where workers contributions form the bulk of the contributions to a plan it should be impermissible for an employer to use the surplus, generated from the worker's contributions, to fund an employer's required contributions to another plan. To permit otherwise would be to allow an employer to effectively transfer its funding obligations for its workers onto the backs of other workers.