



Submission to the Ontario Expert Commission on Pensions

Submitted by the
Ontario Pension Board

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ONTARIO PENSION BOARD
SUBMISSION TO
THE EXPERT COMMISSION ON PENSIONS

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EXECUTIVE SUMMARY

Effective and efficient retirement income systems are critical to our social structure. The current system in Canada features: 1. government sponsored pension plans and social assistance; 2. employer-sponsored pension plans; and 3. individual savings.

Over the past several years there has been growing debate about the most desirable characteristics of effective retirement income systems. The defined benefit ("DB") model is increasingly being called into question.

Ontario Pension Board ("OPB") believes that employer-sponsored DB plans are the most efficient and effective model for delivering retirement security for most individuals. That belief underpins this Submission.

There are other types or models of employer-sponsored plans, including defined contribution ("DC") plans. OPB does not regard the debate around pension plan models as an either/or proposition. There is a continuum of risk sharing and risk pooling along which it is possible to locate reasonably effective plans. There is room for other models. Ultimately, however, OPB believes that delivering financial security in retirement is best achieved by the DB model.

To a great extent, the choice of models is about risk. There is a recent trend away from DB plans to DC plans. The effect is to shift the investment, longevity and other risks from the employer to the employee. There have been a significant number of DB closures in the private sector.

This trend is not in the interests of employees, employers, taxpayers or society at large. We recommend reforms to maintain a robust DB system.

The impact of the trend is about moving away from collective risk pooling to individual risk bearing, and, moving from shared risk between the employer and the employee to the position where the individual employee bears all the risk.

Some individuals are equipped and able to manage that risk. The research shows that most are not. We face a future where the population is ageing in increasing numbers and they may have inadequate financial resources. We think that risk is real and increasing.

The shift in risk has ideological roots. Jacob Hacker puts it this way: *"Today, the message is starkly different: You are on your own. Private employment-based health plans and pensions have eroded, or been radically transformed, to shift more and more*

risk onto workers' shoulders. Government programs of economic security have been cut, restructured, or simply allowed to grow ever more threadbare."

We say, and studies show, there are advantages to the DB model. There is more security and less risk to plan members. There is better workforce management for employers. There are higher investment returns and lower costs to deliver equivalent benefits. There is collective risk pooling. Overall, there is a greater economic benefit to society.

There is a need for rigorous thinking on these matters. The trend away from DB plans does not mitigate risk. It simply moves it and, on a system-wide basis, actually increases risk and cost. Research by behavioural economists shows that people do not manage choice well or at all, often with unfortunate results. The challenges that retirees face are complex and difficult. The point is, properly informed, most individuals should attach a huge value to having a core portion of their retirement income covered within the protective elements of the DB model.

This approach is sometimes called paternalistic. We reject that label. The debate is not about ideology and freedom to control one's own assets and the like. Our society features constructs where we have no input at all, and we accept that. We do not know what drugs are available on prescription, and which are not. Others do. We do not know the protocol for chest pains when we report to Emergency. Others do. If we accept that a DB plan is in part protective, it is no different in principle from other protections we enjoy.

Some industry participants argue that CPP/OAS plans provide adequate coverage. We think that analysis is deeply disconnected from the reality of the lives of many elderly Canadians.

Some regard continuing to work as a reliable retirement plan. Mortality has indeed improved. Morbidity and employability continue to be serious risks that render that approach ineffective for many. Research shows that many more people intend to work during retirement than actually do so.

We move to human error. Nothing eliminates human error. The question is how best to manage that risk. Research shows there are many gaps in personal retirement knowledge and many misperceptions. There are high costs paid by individuals for retirement-related financial services. There is little focus on longevity risk, little interest in financial products to transfer risk and planning is often short-term and intuitive.

We think the DB model most effectively manages these risks. The evidence is clear and consistent. Leaving individuals to fare for themselves is increasingly accepted as an untenable policy approach for a sound retirement income system.

DC plans generally require more dollars of contributions than DB plans to produce the same number of dollars of benefits on retirement. The reasons include: 1. no risk pooling; 2. lower investment returns; and 3. higher investment expense in DC plans. A

recent study holds that the do-it-yourself investor in a DC plan has to save 52.6% more than is needed to fully fund a comparable life annuity through a DB plan. A DB plan is more than 34% cheaper from the point of view of employer and employee combined than a DC plan in providing a comparable benefit.

Most DB plans provide a mandatory retirement savings vehicle. Most provide for mandatory participation while employed and typically prohibit commutation (cashing out) after a certain age. We think this a valuable and protective feature.

DB plans provide low-cost annuitization. If a person is not in a DB plan, the only way to lay off some of the risk is purchasing an annuity. In Canada at least, there is not a very efficient and low cost annuities market. Annuity providers, mostly life insurers, price their products with an expected profit margin. Inflation protection is rarely available. The costs are very expensive. DB plans on the other hand incorporate annuitization directly into the promised benefit. They also operate on a not-for-profit basis.

A DB plan offers powerful incentives for mid-career employees to stay. Unwanted turnover is costly to the employer. A DB plan also offers a mechanism for a desired retirement whether from the employer or employee perspective.

We RECOMMEND that steps be taken to address dissatisfaction with the “pension deal” and establish a clear, certain and balanced approach to risk sharing in DB plans.

1. **We RECOMMEND** that a working group consisting of the representatives of the Plan Sponsor community, the Bargaining Agent community, the Plan Administrator community and other stakeholders be established to develop principles for a risk sharing and funding framework acceptable to the participants.

We offer a detailed set of recommendations. Our general view is that the Plan Sponsor community and the Bargaining Agent community have more in common than what may divide them. A framework can be developed which is, we believe, acceptable to all. Protocols and plan designs can be developed for balanced sharing of systemic risks like life span increases and inflation impacts through mechanisms such as adjusting retirement ages, reserve policies and provisions to permit plan sponsors to recover special shortfall payments from later surpluses.

2. **We RECOMMEND** that the applicability of trust law principles to pension plans should be reviewed and clarified.

The issue of the applicability of trust law principles to DB plans is inseparable from the issues of risk sharing and funding. The review should be conducted on an issue by issue basis. The strict application of these principles has restricted employer access to excess or surplus funds. This creates a disincentive to creating and maintaining an employer-

sponsored plan. Trust law however has usefully protected plan assets in the event of an employer bankruptcy.

The application of trust law principles in the pension context has created complexity and uncertainty in relation to questions dealing with surplus withdrawals, plan mergers, contribution holidays and paying expenses from a plan.

We observe that classic trust law does not easily translate to the pension context. The pension plan context is essentially a component of the contractual employment relationship between employer and employee.

Therefore, where appropriate, the PBA should be amended to reflect whether trust law principles ought to be applied with respect to a particular issue. This approach is consistent with the Supreme Court of Canada's decision in Buschau v. Rogers Communications Inc. This approach also results in the legislature making pension policy on key issues, which OPB submits is the proper result.

We RECOMMEND that steps be taken to address the perception that DB plans involve unmanageable risks for employers.

There is a real perception among employers that DB plans impose unmanageable costs and risks on the employer. There are practices and technologies available to manage the funded status of the plan. Using cautious assumptions, applying cautious analysis to benefit improvements, adopting a strong reserve policy and strong and effective reporting are relevant. There are approaches to regulatory oversight of risk management that are used with respect to federally-regulated insurers. It would be useful to review those approaches and consider their utility in managing pension plan risks.

We RECOMMEND investigating methods of building incentives for employers to sponsor DB plans to balance the impact of globalization and short-termism in the capital markets.

Business organizations are increasingly global. Competition comes from jurisdictions where labour costs are low. There is severe pressure to reduce labour costs.

Corporate goals and capital markets frequently focus on short-term performance. Changes in accounting rules have increased the volatility of the income statement. Smoothing of assets and liabilities has largely been eliminated. The funded status of DB plans is subject to considerable volatility. There is a mismatch here: the market emphasis on short term performance is at odds with the long-term perspective necessarily required to properly manage a DB plan.

There is a real benefit and value to society and taxpayers from broad DB coverage. That value should be recognized and shared with employers who sponsor DB plans.

Cost certainty is an issue. A regime and environment that encourages "proper funding" of a DB plan goes a long way towards creating some level of certainty.

We RECOMMEND taking steps to level several aspects of the regulatory playing field for DB and DC plans.

1. **We RECOMMEND** that DC plans be required to measure and report to members on expected retirement income levels and adequacy of their DC assets.

This is not so now, and in our view, ought to be a requirement.

2. **We RECOMMEND** the *Pension Benefits Act* (the "PBA") should be amended to require some level of mandatory annuitization in primary employer-sponsored DC plans. The Government should develop an approach to enable the development of a large annuitant pool and a not-for-profit/low cost annuity provider(s).

As previously observed, the DB model offers a pooling of investment, longevity and other risks. The DC model does not. A challenge to the DC model is the low level of annuitization which is a result of poor understanding of annuities and the high cost of annuities in Canada.

There should be a method of providing life income that enables the guarantor of the income to have a reasonable risk pool and to manage efficiently.

This recommendation could also help to provide greater portability of private sector DB benefits, the lack of which is an impediment to broad DB coverage in the private sector.

3. **We RECOMMEND** that the specific issues relating to insufficient regulation of DC plans and other retirement savings vehicles be addressed.

There is a different level of scrutiny that is applied to DB plans than is applied to DC plans. This makes no sense if one of the primary objectives of the PBA is consumer protection. We support the regulation of DB plans with a view to protecting plan members. However, DC plans pose risks to plan members as well and should be regulated accordingly. That discussion may need to be extended to group RRSPs to level the playing field.

We RECOMMEND taking steps to increase appreciation for the value of DB plans among employers and employees.

The value of the DB plan for employers and employees is supported by research but there are very low levels of understanding of that value among employers and employees.

The factors in play are:

- For employers, the main benefits are attracting and retaining top quality talent and effective and efficient workforce management. A DB plan can be a competitive advantage in a global economy and a tight labour market. DB plan coverage will also be an important tool in a world without mandatory retirement. This is not appreciated by employers.
- For employees, there is a lack of understanding and appreciation with respect to the value of a DB plan. One reason is a lack of educational effort by employers, plan administrators and the regulator.
- The wealth management industry devotes substantial resources promoting the value of the DC model.
- OPB has made education on these issues a core strategy. Others are moving in that direction.
- The Government can and should support these initiatives. Encouragement with respect to broad coverage should be a mandate of FSCO.

We RECOMMEND fixing inflexible DB to DB transfer rules.

Sections 80 and 81 of the PBA apply to divestments/restructurings, mergers and acquisitions. These sections should be amended to:

1. Enable members transferred from one pension plan to another in connection with a divestment to elect to consolidate their pension credit in the pension plan of the transferring employer into the pension plan of the transferee employer;
2. Enable the pension plans to enter into transfer agreements which provide for credit and asset transfers that protect the value of the benefit accrued in the transferring plan; and
3. Preserve the other rights of affected members currently afforded under Sections 80 and 81.

We RECOMMEND developing a multiple employer DB platform which would facilitate participation by small and mid-sized private sector employers.

Small businesses are a major employer in Ontario. Very small DB plans lack economies of scale and are prohibitively expensive. A solution may be the multiple-employer model that is prevalent and successful in the public sector in Ontario. These plans have common characteristics:

- Administration by independent special purpose agencies.
- Good economies of scale and professional staffs.

- Administrators governed by capable trustees/boards.
- Covering employees of a number of employers, including many small employers.
- DB plan designs with good benefits.
- Contributory plan design and accordingly a built-in sharing of risk.
- Strong commitment by plan stakeholders.
- Longevity, investment and disability risks are fully pooled.
- Spousal survivor benefits are provided.

We RECOMMEND taking steps to bolster both the actual and perceived security of the DB pension promise.

There have been a small number of high profile DB plan failures. Troubled industries like steel and airlines are examples. The fact is, these are rare events. The DB promise is, and will continue to be, fully delivered by the vast majority of plans. This message is not accurately communicated or communicated at all. There is no strong voice delivering this message. FSCO is not engaged. There is no DB-dedicated industry association in Canada.

OPB does believe that a safety net is essential and we therefore recommend continuance of the Pension Benefit Guarantee Fund.

We RECOMMEND that FSCO be provided with a legislative mandate to encourage broad coverage by employer-sponsored plans.

FSCO has no mandate to encourage broad coverage; it should have, in our view. FSCO should have a strong role in bringing stakeholders together to resolve challenges facing the DB model and in providing the proper perspective on the security of the pension promise.

We RECOMMEND the PBA be amended to remove certain prescribed quantitative investment restrictions that impose unnecessary constraints or have become outdated and are no longer practical.

Subsection 22 (1) of the PBA imposes the "prudent person rule". This is a guiding principle and OPB supports it.

An example of an outdated rule, in our view, is the "30 % Limit". That rule precludes investing assets in securities of a corporation to which are attached more than 30 % of the votes that may be cast to elect directors of the corporation. The rule was in place when pension funds were largely passive investors and were much smaller in size. With the growth in size and a switch to more active private equity strategies, the rule has become problematic. The imposition of the "prudent investor" standard is an adequate regulatory control.

We RECOMMEND amending the rules for the division of defined benefit pensions on marriage breakdown.

The objectives are finality or certainty at the time of division, permitting the spouse who is not a member of the pension plan to keep his or her share of the benefit in the plan, cost neutrality, ease of administration and clarity for members as to amounts and value.

The Family Law Act and PBA regimes governing the division of pension benefits are extremely complex.

As an example, there is a contradiction between Sections 44 and 48 (13) of the PBA. Section 44 indicates that if separation occurs before retirement, and the pension commences at retirement, and the member later dies, the post-retirement benefits are not payable to the spouse. Section 48 (13) expressly permits the assignment of pre-retirement death benefits. The assignment of post-retirement death benefits should be expressly permitted. It is not equitable that the timing of the member's death determines the entitlement of the member's former spouse.

Section 51 (2) provides that the member's spouse cannot receive more than 50 % of the accrued pension benefit during the period when the parties were spouses. There have been cases where 100% of the member's pension was payable to the spouse. OPB is opposed to such "stacking". We view the 50% rule as good public policy. The issue needs to be clearly addressed.

OPB would support a division scheme where the non-member spouse may elect to become effectively a member of the plan. OPB would support an approach which enables the non-member spouse to elect to receive either a lump sum or a pension benefit.

We RECOMMEND that the roles of all industry stakeholders be clarified.

The PBA should clearly specify the roles and duties of the affected parties. We believe that DB Plan Administrators should be subject to an express duty of care to take reasonable steps to protect the long-term health of the plan. Advisors should be subject to a similar duty. The question of a potential conflict should be addressed where an advisor such as an actuary provides services to both the plan sponsor and the plan administrator.

We RECOMMEND that financial advisors providing services to a client who is a member of an employer-sponsored plan should be regulated.

OPB is concerned that many financial/investment advisors appear to be operating under little or no rules or regulatory supervision in luring members to cash out of their DB plan with promises of greater returns. They are in a conflict of interest situation with great power over their vulnerable clients – the classic circumstances for the imposition of fiduciary duties.

We RECOMMEND the current locking-in and commutation/transfer rules be maintained.

Under the current PBA regime, benefits are locked in after two years. We believe that regime should be maintained. The existing exceptions in our view provide sufficient flexibility. Locking-in is consistent with the fundamental purpose of a pension plan – to provide retirement income.

OPB also supports the current PBA regime which does not require that portability be offered to members who are entitled to an immediate pension from a plan. This is consistent with the research that demonstrates that the optimal approach is to annuitize a significant portion of one's assets, even for high net worth individuals.

We RECOMMEND a working group consisting of plan sponsors and organized labour be created to develop solutions to current issues that would support the DB model.

We believe this can be done. We also believe if the recommendations ultimately made by the Commission are supported generally, the likelihood of implementation increases.

**ONTARIO PENSION BOARD'S SUBMISSION
TO
THE ONTARIO EXPERT COMMISSION ON PENSIONS
OCTOBER, 2007**

WHO WE ARE

Ontario Pension Board ("OPB") is responsible for the administration of the Ontario Public Service Pension Plan (the "Plan"), and for the prudent investment of the assets that fund the Plan (the "Fund"). The Plan is a statutory pension plan established by the Public Service Pension Act ("PSPA") and is Schedule 1 to that Act. The terms of the Plan are set, and may be amended, by Order-in-Council, not by OPB. As at December 31, 2006, the Fund had assets of \$15.75 Billion.

OPB provides pension related services to approximately 34,600 active members, 4,800 deferred members and 36,900 pensioners and their survivors. Its membership is made up of eligible employees of the Ontario Government and its Agencies, Boards and Commissions. The other key stakeholders of the plan are the Plan Sponsor (the Ontario Government), several Bargaining Agents that represent members in the Plan and the taxpayers of Ontario.

The Plan is a defined benefit pension plan, meaning that its members, upon retirement, receive a monthly pension payment and other benefits, the amounts of which are based on each member's years of service and level of salary. The Plan is a contributory plan and the normal contribution rates made by members and participating employers is 6.2% of salary up to the Year's Maximum Pensionable Earnings under the CPP and 8% of salary above that amount. The pension benefit provided by the Plan is indexed up to 8% in any given year with any excess carried forward to future years.

The Plan is one of the largest and oldest defined benefit plans in Canada. OPB was established in 1990; however, the Plan has been in existence since the 1920s.

INTRODUCTION

Pensions and health care are two of the most important conversations taking place in Canada today. As the population ages, more and more Canadians are concerned about making sure they have sufficient income and resources for their retirement years. Over the past several years there has been growing debate about the most desirable characteristics of effective retirement income systems. The defined benefit model is increasingly being called into question. Many employers in Canada, the U.S., and the U.K. are re-evaluating their commitment to defined benefit pension plans and the form that their support for retirement security may take. The growing focus on pensions has governments and policymakers under pressure to respond with policy initiatives that will encourage and sustain pension coverage that supports the needs of both individuals and employers. This has led the Ontario Government to establish the Expert Commission on Pensions to review the legislative environment for defined benefit plans. OPB commends the Government for taking this initiative.

Three Pillar Retirement Income System: Canada's current retirement income system is built on three pillars. The first is government-sponsored plans and social assistance (CPP and OAS). The second is employer-sponsored pension plans. The third pillar is individual savings. This submission is about the second pillar and in particular employer-sponsored defined benefit ("DB") plans. Many Canadians enjoy a secure retirement and a regular income in retirement today because of employer-sponsored DB plans. Pension benefits are important to these Canadians and their families. DB plans also meet many of the needs of different stakeholders – employers, shareholders and society at large.

OPB's Beliefs: OPB believes that:

1. employer involvement in the retirement income system is as essential as universal health care to maintaining the social fabric of this country;
2. a three pillar system in which each pillar is robust delivers an ideal mix of sources of retirement income;
3. employer-sponsored DB plans are the most efficient and effective model for delivering retirement security to most individuals; and
4. employer-sponsored DB plans can be a competitive advantage for employers in a global economy and a tight labour market.

These beliefs underpin our submission.

OPB believes that it is essential to have a legal and regulatory environment that supports robust employer-sponsored DB coverage as part of Ontario's retirement income system. The Government of Ontario clearly shares that belief. In establishing the Ontario Expert Commission on Pensions the Government directed the Commission to observe, as one of its guiding principles, "*the importance of maintaining and encouraging the system of defined benefit pension plans in Ontario.*"

We hasten to say that, while we strongly support the features and benefits of the DB model, we also believe that other models of employer-sponsored retirement income plans can be effective and have a place in the system along side a robust DB system. We also want to be clear that we do not regard the discussion around employer-sponsored pension plan models as an “either or” discussion. There is, between the two traditional types of employer-sponsored pension plans (DB and defined contribution), a continuum of risk sharing and collective risk pooling along which it is possible to locate reasonably effective alternative plan design structures. Ultimately, our point is that, with some modifications to the current environment in this province and federally, the employer-sponsored DB model will be the most efficient and effective way to deliver financial security in retirement to Ontarians. It deserves a great deal of tender loving care from our legislators.

As we will discuss in this Submission, we are concerned that the regulatory playing field is tilted in favour of the DC model. The playing field should be level.

OPB welcomes the opportunity to make a submission to the Commission. Our submission is in several parts.

- First, there is a downward trend in defined benefit plans that has emerged in recent years.
- Second, this is not in the interests of employees, employers, taxpayers or society at large.
- Third, we recommend reforms to encourage robust defined benefit coverage in Ontario.

THE RISK IS SHIFTING: THE DRIFT AWAY FROM DEFINED BENEFIT PLANS

The Drift Away from DB: Pension plans have changed in recent years. In parts of the world there has been a significant shift away from DB plans in the private sector and a small number of instances of DB plan closures in the public sector. This shift has been very strong in the U.K. and the U.S. with a similar, although not as rapid, shift in Canada.¹ The drift away from DB plans in Canada in the private sector does appear to be accelerating. Within the last 24 months Sears Canada, Nortel and BCE have announced the closure of their DB plans. In the majority of cases the shift involves the closure of the DB plan (in some cases to new entrants with existing members permitted to continue to accrue and in other cases a freeze on any further accrual) and replacement with a defined contribution (“DC”) plan (for the purposes of this submission, we include in DC group RRSP plans and other individual account type plans). During the 1990s and early 2000s the number of members covered by DB plans in Canada slid sharply.²

Furthermore, the models used by other industrialized countries in their government-sponsored plans (the first pillar) has also shifted away from the traditional DB model to the DC or some form of hybrid model (“Hybrid”) – that is, a combination of the DB model and the DC model.³ Under the DC model, an individual has an account into which contributions are made. The employer provides a menu of investment options from

which the individual may choose. The individual bears the investment risk. Upon retirement the individual has a fund totaling the contributions that have been made plus whatever investment returns have been earned on those contributions. In the vast majority of cases, the individual is then left to determine how to convert that fund into a stream of income that will last for the individual's and any spouse's lifetime.

In many cases DC plan members do not fully understand the investment risks they are assuming. According to a John Hancock Financial Services Defined Contribution Plan survey⁴ conducted in 2002 (the Eighth in a series) 90% of respondents realize that they could potentially lose money in a stock fund, however nearly 40% did not realize that they can lose money in a bond fund. This survey also found that respondents long-term (20 year) return expectations were unrealistic. Survey respondents expect returns over 20 years as follows:

- Stocks/Equities 15.8%
- Bonds 10.3%
- Money Market 9.8%.

Impact of the Trend away from DB: What is very clear from this is the shift:

- away from collective risk pooling to individual risk bearing; and
- away from the employer bearing some of the risk to the individual employee bearing all the risks.

The impact of the shift is a big increase in individual responsibility. Some individuals are equipped to deal with that responsibility, but, as the evidence discussed below clearly demonstrates, many are not. We are human. The point of a DB plan is to provide a proper structure for effectively managing the responsibility on behalf of individuals. In a recent study, the Canadian Institute of Actuaries (CIA) found that 2/3rds of Canadian households that are expected to retire in 2030 are not saving at levels to meet required living expenses. They also found that workplace-linked pensions are the most promising way to fill the gap.⁵ The message is that coverage by employer-sponsored plans, and particularly DB plans, needs to be increased. The result of a continued drift away from DB will be a decline in retirement security for many individuals at a time when the proportion of elderly in society will be at an all time high. There is real reason to be concerned that we are facing a future in which the degree to which the elderly find that they have inadequate financial resources is unacceptably high.

An Ideological Cause: A major part of the reason for this drift away from DB is an ideological shift that has occurred. Defined benefit pensions and social security systems have been based on the idea that collective risk pooling is important in society. Today many people in positions of influence oppose collective risk pooling and focus on individual responsibility as the path to security. There is an attitude that retirement planning responsibility and ownership belongs with individuals. This is discussed in *The Great Risk Shift* by Jacob S. Hacker.⁷ The following remarks are made in a U.S. context, the general direction, we believe, remains applicable in Canada.

“The Great Risk Shift is not just an economic change; it is also an ideological change. For decades, Americans and their government were committed to a powerful set of ideals – never fully achieved, never without internal tension – that combined a commitment to economic security with a conviction that a strong economy and society hinged on basic financial security, on the guarantee that those who worked hard and did right by their families had a true safety net when disaster struck.... Today, the message is starkly different: You are on your own. Private employment-based health plans and pensions have eroded, or been radically transformed, to shift more and more risk onto workers’ shoulders. Government programs of economic security have been cut, restructured, or simply allowed to grow ever more threadbare.”

In addition, the evolution of new perspectives as to the “right” way to think about pension finance is reinforcing this perspective. Financial economics is based on the notion that the interests of the shareholder should be predominant in thinking about how to organize pensions.

Essentially, the "mark to market" approach advocated by financial economics will lead to the destabilization of the funding of DB pension plans and hence accelerate the abandonment of those plans. That result, together with the deficiencies and inefficiencies in the DC plans discussed in this submission, will lead to increasing pressure for the expansion of the direct role of the state in providing for retirement security.

Financial economics has another impact. We believe that the ideological perspectives underlying the approach lead some discussants of pensions issues today to overlook many of the advantages of the DB model. In financial economics and options pricing models, that which cannot be measured has no value. Financial economists do try to value some of the “soft” attributes of DB plans but we suspect they are undervalued given what the evidence shows regarding the challenge individuals face in managing their retirement planning.⁸ Certain other aspects of the DB model are not included in financial economics models. Financial economics fails to consider the added value created by plans that operate without participants needing to take action. Such plans do not depend on participant knowledge and foresight to produce desired results, but they may suffer from lack of appreciation, particularly at early career stages. Financial economics is focused on optimizing the interests of rational shareholders and fails to consider that many individuals are not shareholders and if they are, they are not rational planners. The point is that, as with the results of all mathematical models, conclusions drawn from financial economics need to be approached with caution and an overlay of judgment about the real world. In our view, most financial economics analyses of the DB model undervalue it relative to the risk of leaving retirement planning to individuals.

THE ADVANTAGES OF THE DB MODEL

A good and efficient retirement system is important to society. Employer-sponsored pension plans increase the financial security of older workers and pensioners. With this comes increased dignity and self-sufficiency in retirement and less reliance on government social security programs. A good DB plan provides protection from

adversity and shocks in the form of disability or premature death as well as for the individual who personally, or whose spouse, lives a long time.

As many employers shift to DC plans, employers and employees lose many of the advantages of DB plans. There are inherent advantages in the risk pooling and collective purchasing that are present in DB plans. Some discussants of pension issues today have lost sight of the benefits of DB plans in their focus on the risks they present to employers. A number of recent studies have listed the advantages of the DB model.⁹ The CIA in its submission to the House of Commons Standing Committee on Finance stated that defined benefit plans are in the best interest of Canadians.¹⁰ The CIA presents a number of reasons for their statement. Some of the more important reasons are:

- more security and less risk to plan members,
- better workforce management,
- higher investment returns,
- greater economic benefit to society and the economy, and
- better pension coverage for employees in all sectors.

Below, we discuss in some detail several of the most important advantages of the DB model.

There is a need from more rigour in the discussion of pension plan models: Before doing that we want to address the need for more rigorous thinking about the rationale for, and the impact of, the shift away from the DB model. Part of the rationale for the shift away from DB is a straightforward move by employers to unload risk and cost. That rationale does not consider the benefits of a good DB plan to the employer and it also considers only the interests of one of the stakeholders and ignores the interests of employees and society as a whole.

The need for more rigour shows up in several other areas.

- ***The trend away from DB does not mitigate risk or reduce cost:*** First, the shift away from DB is often presented and accepted as a system-wide solution; as though the DB model actually creates the cost and risk and moving away from a DB plan and shifting the risk actually reduces the cost and makes the risk disappear. That is clearly not right. In fact, it is virtually certain¹¹ that the system-wide (total) cost and risk increase with the shift away from DB. Abandoning collective risk pooling actually increases the aggregate cost since each individual has to pay the maximum price for bearing the risks (i.e. outliving funds) or offloading some or all of them (i.e. annuitizing). It also increases the risk since all the empirical evidence shows that many individuals do not manage these risks well. The evidence is that in DB Plans (excluding small DB plans) investment returns are higher and investment management fees are lower than in DC plans (the cost/return figures are even worse for individuals who are entirely on their own). The point is that pooling of risk and achieving

economies of scale in investment management is an economic decision that has extremely high returns.

Moreover, the very same factors that lead employers to be concerned about the financial burden of a DB plan operate equally on individual retirement savings accounts. Low interest rates, earlier retirement, longer lives, the apparent reduction of the equity risk premium and the challenging investment environment all have the same impact on individuals as they do on DB plans: they increase the pool of capital required to confidently fund a given level of lifetime retirement income. Financial economists and the risk management profession have developed very sophisticated tools to analyse levels of risk and the price of risk. These tools and principles do not get applied to the discussion of the system-wide impact of the shift away from DB.

We think it highly probable that the aggregate under-funding in DC plans significantly exceeds the aggregate funding shortfalls in DB plans. There is no regulated requirement to measure and report the adequacy of the assets in DC plans similar to that in place for DB plans, so the under-funding in DC plans is unknown. This rarely seems to be recognized in the discussion. Of course, the fact that it is unknown does not make the problem go away. It simply defers having to deal with it until it hits us. Later in this submission, we recommend that an adequacy measurement and reporting requirement be added to the regulation of DC plans.

- ***DB plans are appropriately and necessarily “protective” not “paternalistic”:*** The concept of paternalism often arises in discussions of the DB model. It is put forward as a reason to reject the model. The arguments advanced focus on controlling one’s own assets, determining one’s own future and the like. These arguments derive from a political philosophy and a particular world view. They are, in our view, wrong when they are applied to the DB model. We are all free to make a virtually unlimited range of personal choices. We can buy two lottery tickets on the same event. We know the odds do not change but the capital investment just doubled. But if we want to do it we can. If we are truly foolish (or having fun), we can bet on the Maple Leafs to win the Stanley Cup. We are also regulated in our lives in a hopefully beneficial way. Few of us know what drugs are available on prescription and which are not. Others, with the expertise, determine that for us. We accept and trust in that. Few of us know the protocol when we report to Emergency with chest pains. We, again, accept that the experts do know and we have faith in that and act accordingly. If we accept that the DB model is protective, then the protection is no different in principle from the constructs we create in many areas of our society.

Research by behavioural economists shows that people do not manage choice well or at all, often with quite unfortunate results. Sophisticated

investors know that asset allocation is one of the primary drivers of investment return and that it is one of the most challenging decisions to make. Yet a model that shifts the investment responsibility onto the individual leaves that decision to the individual. The wealth management industry is now introducing “lifecycle” investment vehicles that remove much of the choice and control over investments from the individual.

The research done to date on the problems with choice have focused on how well active employees manage investments. However, the difficulty of successfully managing one’s financial retirement surely increases dramatically with age. Feelings of isolation, vulnerability and lack of confidence in many elderly can make this an overwhelming challenge. Most are painfully, keenly aware that they cannot afford to make a mistake. Moreover, the management challenge that retirees face is infinitely more complex and formidable than the saving level and investment management challenges faced by active employees. Retirees have to devise and execute a plan to achieve decent investment returns while drawing down their assets in retirement with a view to ensuring an adequate lifetime income for themselves and their spouse. The only way to offload that challenge and the risk of failure in meeting it is through annuitization which is very expensive and very mysterious to most. There is far too little research into this important area of retirement planning.

The point is that all the research leads to the conclusion that, properly informed, most individuals should attach huge value to having at least a core portion of their retirement income covered within the type of protective elements that are part of the DB model. The desire for such things as individual control and leaving money to one’s heirs can and should be addressed outside of and alongside a DB plan. In fact, having reliable income from a DB plan should better enable individuals to arrange their affairs to leave an inheritance to their loved ones. A very recent study from the Pension Research Council strongly supports this.¹² All of this seems to be recognized rarely, if at all.

None of this is a criticism of the elderly or the aging. Growing old is a fact of life. It is a process with predictable consequences. It is a fact that we respect. That respect drives our conclusion that the protective components of the DB model are essential.

- ***CPP/OAS do not provide adequate coverage:*** Third, we note that some industry participants argue that the current CPP/OAS programs provide adequately for most Canadians. The analysis that leads to that conclusion is deeply disconnected from the reality of the lives of many elderly Canadians. For example, it appears to completely ignore the financial demands of the increasing cost of health care for elderly Canadians. Many elderly couples face a reality in which one of them needs to be placed in a long-term care facility but the other is quite able to continue to function

entirely independently. Those with little more in the way of financial resources than CPP/OAS simply do not have the option of arranging their affairs accordingly. Others are faced with the cost of care for disabled children. It simply is not acceptable to judge the adequacy of CPP/OAS on the basis of the sunniest-possible-day-scenario for the elderly.

- ***Continuing to work is not a reliable retirement plan:*** Fourth, there seems to be a view that continuing to work is a reliable fallback for those who have not made adequate provision for their retirement. The problem with that thinking is that it leaves individuals and their spouses wide open to morbidity and employability risk. And the research suggests that, though mortality has indeed improved, morbidity and employability continue to be serious risks that increase as one approaches retirement.¹³ Many more people intend to work during retirement than actually do so.¹⁴

In fact, in a recent report¹⁵ published by the Society of Actuaries (April 2006) they found that approximately 40% of those who intended to continue working end-up retiring earlier than planned. The survey cites three main reasons for the earlier retirement:

- i) health problems or disability;
- ii) looking after an elderly family member;
- iii) job loss.

- ***Nature of DB plan is no more open to gaming and agency risk than any other model:*** There have been suggestions that the DB model is flawed because the system is gamed by the stakeholders and that the gaming cannot be prevented. Categorically, that has not been our experience as administrator of the Public Service Pension Plan. Both the Government of Ontario as Plan Sponsor and the several Bargaining Agents that represent members of the Plan are very responsibly focused on protecting the long-term health of the plan. They are, we say, exemplary pension plan stakeholders. We believe that OPB's governance model, which engages stakeholder participation through the representation on the Board of nominee Directors of the Plan Sponsor and each Bargaining Agent combined with unaffiliated members, contributes to the positive environment. We have every reason to believe that many other pension plans operate in a similar constructive environment.

Moreover, it is wrong to suggest that other pension plan models are any less subject to gaming and agency costs. DB plan administrators take their fiduciary duties very seriously and use their scale and sophistication to manage agency risk very effectively. DB plan administrators are under constant pressure to become "High Performance Pension Delivery Organizations".¹⁶ We agree with that movement. While gradual, it is improving the performance of DB plan administrators. DC plans, by nature, do not have strong plan administrators to look after the interests of

plan beneficiaries. In fact, many DC plans do not provide any assistance to the individual with annuitization or drawing down their assets in retirement. In short, we believe that agency risk in DC plans is at least as high as in DB plans.

In the remainder of this section, we move onto a discussion of some of the advantages delivered by DB plans.

DB Model Most Effectively Manages Human Error Risk

The DB Plan model is managed by informed experts in investments, day-to-day administration and plan design that better manages the risk of human error. Keith Ambachtsheer in *Pension Revolution*¹⁷ points out flaws in DC plan operations.

“First, behavioral finance research confirms that most people are hesitant, inconsistent, even irrational planners and decision makers regarding their own financial future. Second, informational asymmetry and misaligned interests with regard to the global for-profit financial services industry drive a material wedge between workers and the retirement money they do accumulate. The result is that many workers pay too much for the retirement-related financial services in relation to their true economic value. These excessive fees paid over a working lifetime are another important factor why so many workers are under-achieving their pension goals. The third DC plan flaw is that these arrangements leave plan members bearing the full burden of longevity risk. Surely we should not expose the many millions of retirees around the world to the material risk of outliving their assets.”

There are many gaps in personal retirement knowledge and many misperceptions. Repeated studies from the Society of Actuaries, Employee Benefit and Retirement Institute (EBRI), Life Insurance and Market Research Association (LIMRA) and Mathew Greenwald and Associates document these gaps and misperceptions. Surveys of knowledge of post-retirement risk have been conducted four times, in 2001, 2003, 2005 and 2007. Some of the key issues these studies highlight are as follows:

- There is relatively little awareness of and focus on longevity risk.
- The main method of managing assets to prepare for risk is to reduce spending.
- There is relatively little interest in the use of financial products to transfer risk.
- Planning at time of retirement is often short-term and intuitive.
- There are gaps in knowledge about post-retirement risk and this does not seem to be changing much.

As part of this research, the Society of Actuaries and LIMRA worked together to do focus groups with individuals who had retired with balances of \$100,000 to \$500,000 in employer sponsored DC plans (401(k) plans for most). Participants were between 60 and 72 and had retired two to ten years earlier. They were selected at least two years after retirement so as to have given them time to put plans and investments in place. The report includes many quotes from the participants and provides a sense of how people

think about the issues surrounding retirement. Here are sample quotes from participants:¹⁸

- I didn't consider how long retirement would be." (page 11)
- I thought you were supposed to retire when you were 65 and I thought I would try it." (page 12)
- "We take it day by day... I can't worry about what is going to happen tomorrow." (page 14)
- "If I want it, I buy it." (page 17)
- "I spend a lot more money than I thought I would spend, mostly entertaining myself." (page 17)

These quotes certainly do not represent all retirees. But it does reflect a profound theme shared by most individuals. Far too many are intuitive, ad-hoc, and not thoughtful as they plan for retirement.

A study from SEI Investments in Canada¹⁹ finds gaps in knowledge among DC plan participants in Canadian based DC pension plans. It states:

"Employees are also unclear on many of their DC plan features. For example, 75% of employees surveyed believe they can make their own contributions to their pension plan, when in reality, only 51% of organizations allow them to do so. In addition, only 39% of employees correctly knew that their pension plan is compulsory. In reality, 71% of members are in compulsory plans."

There are many other studies and pensions experts who have come to the same conclusion. For example, in his recent book *Pension Revolution*, Keith Ambachtsheer²⁰ discusses the "Human Foibles" that inhibit individuals from successfully managing their own retirement planning. In their book *Pension Design and Structure*, Olivia Mitchell and Steven Utkus list six challenges that individuals face in managing their own retirement planning and assets.²¹ A Society of Actuaries Report²² lists ten key misperceptions that individuals suffer from and that inhibit their ability to manage their retirement plan well.

The evidence is clear and consistent. Leaving individuals to fare for themselves is increasingly accepted as being an untenable policy approach on which to create a sound retirement income system.

DB Plans Deliver a Given Level of Retirement Income at Lower Cost

DC plans generally require more dollars of contributions than DB plans to produce the same number of dollars of pension benefits once people retire. The only exception to this is that very small DB plans have proportionately higher administrative costs than large DB plans or DC plans.²³

Therefore the shift away from DB can lead to higher costs or less security in retirement or a combination of the two. The higher costs are the result of several different forces interacting:

- Lack of risk pooling – if one wants a reasonable certainty of not outliving assets, more money is needed when risks are not pooled.
- Lower investment returns.
- Higher rates of investment expense in DC plans.
- In addition, DC plans result in great variation in results by individual, so that if benefits are lower on average, some people will receive much lower benefits than the average.²⁴

The difference in cost between a DB plan and DC plan for the same retirement result has been estimated in a recent study.²⁵ The findings were as follows:

“The do-it-yourself investor in a DC plan, then has to save 52.6% more than is needed to fully fund a comparable life annuity such as can be obtained through a DB plan. Thus, a DB plan is more than 34% cheaper – from the point of view of the employee and the employer combined – than a DC plan in providing a comparable benefit. Recognizing the sales costs, discount rate, profit spreads, and annuity table biases that may all be present in commercial annuity prices but which are not present in an annuity from a DB plan, it is possible that we have underestimated the savings.”

The same report also explains the advantages in the DB Model that lead to these savings:

“The lagniappe to be shared by both the sponsor and the participant comes from, in order of importance:

- *Sharing of mortality risk through the magic of the Insurance Principle, which reduces the level of savings required to provide a lifetime income.*
- *Avoidance of high fees and other costly biases that are unavoidable in commercially available life annuities.*
- *Access to investment products at institutional (wholesale) rather than retail levels of investment fees and other costs.*
- *Management of the investments by skilled professionals rather than by the individual.”*

While we do recognize that collective purchasing can be achieved to a meaningful extent in other models of pension plans, at equivalent sizes, DB plans are most effective in that regard.

A number of studies have concluded that the cost of DB plans is substantially lower than that of the DC model. Mercer provided a perspective focused on the private sector employer-sponsored plans in its *Defined Benefit Plans: Still a Good Solution* (written by Don Fuerst, F.S.A, A Mercer Perspective on Retirement, April, 2004, Mercer Human Resource Consulting, New York, New York). This paper shows how DB plans create

value. The paper demonstrates that for 6% of pay contributed to a DB plan, the employee hired at age 30 gets a benefit that would require an 11% pay contribution to a DC plan. This assumes that both the DB and DC Plans invest in risk free long-term bonds and that benefits are equivalent at retirement at age 65.

DB Plans provide a Mandatory Retirement Saving Vehicle

In order for most individuals to have any prospect of saving enough to provide for a reasonable level of replacement income during retirement, they need to start saving early and continue to do so throughout their working lives. Given the human foibles to which many people are subject, they fail to do this, as confirmed by the CIA report referred to above. Some do not save at all for retirement. Some who do, cash out and use their retirement savings for other purposes. DB plans typically provide for mandatory participation while employed and prohibit commutation (cashing out) of the accrued benefit after a certain age. This mandatory participation aspect of DB plans is very valuable.

Benefit adequacy

Most defined benefit plans are designed to generate a reasonable level of replacement income. They do a very good job of doing so relative to other models. Many provide disability pensions and spousal survivor benefits. *The Fidelity Retirement Index* in the UK reported, in May, 2006, that:

“the savings and State benefit entitlements of typical DC plan holders will, on current trends, replace just 38% of their expected final earnings once they reach retirement. ... DB scheme members are on course to replace 81% of their expected final earnings.”²⁶

The point is that there is no free lunch in retirement planning and that contribution rates by both employers and employees are too low in many DC plans to generate adequate retirement income. In another study, Fidelity in the UK concluded that, *“Those who believe that DC plans cost less may fail to recognize that they also deliver much less retirement income.”²⁷* Generally, contributions need to be higher in DC plans than DB plans to generate a given level of retirement income. Many of the factors that have led to the need for higher contributions to DB plans surely have the same impact on the contributions needed for DC plans to provide an adequate level of retirement income.

It is important to recognize that many DC plans fail to focus on benefit adequacy and fail to provide information about the income the plans can provide to help the participants plan for retirement. Account balances are usually provided, and many participants do not know how to translate them to regular income and evaluate their purchasing power during retirement.

DB Plans Provide Low Cost Annuitization

The only way most individuals have of effectively managing longevity and investment risk during retirement is to lay off at least some of that risk by buying an annuity. Therefore, for the retirement income system to operate properly for individuals who are not in DB plans, it is essential that there be a very efficient and low cost annuities market. But robust, well-functioning voluntary annuity markets do not exist in Canada or, for that matter, in any other country with the possible exception of the United Kingdom.²⁸ Annuity pools are generally small, leading to higher costs. Of course, annuity providers, mostly life insurers, price their annuities with an expected profit margin. As a consequence annuities are expensive and the range of annuity products available to Canadians is limited. For example, inflation protection is offered only by a few providers and is essentially prohibitively expensive.

DB plans incorporate annuitization right into the promised benefit. Reasonable sized DB plans have large pools resulting in more predictable demographic experience. They also operate on a not-for-profit basis.

DB Plans Provide an Effective Human Resource Management Tool

DB plans also help employers manage their work forces better, thereby improving productivity. DB pensions offer powerful incentives for mid-career employees to stay with employers until retirement eligibility. Unwanted turnover can be costly. Some experts have estimated that replacing an employee can cost a year's salary or more. This varies by job and employer.

When the employer wants an employee to retire or a longer service older employee wants to retire but, in either case, the employee cannot afford to, it creates a difficult problem for both the employer and employee. In privately owned businesses, this creates a negative situation for shareholders as well. With the elimination of mandatory retirement in Ontario, this feature of DB plans is likely to be highly valued by employers and employees in the years to come.

In addition, in a situation of employment downsizing, DB plans can be a helpful tool to cushion the effect on older workers.

Capital market perspective

David Dodge, Governor of the Bank of Canada, has focused on the importance of DB pensions to the Canadian capital markets. He said:

“Pension plans generate important benefits in terms of economic efficiency. By transferring risk from individuals to collectives, pension plans help achieve a more efficient allocation of savings. Pension plans — particularly the very large ones — tend to have sophisticated asset managers. These large plans have the incentive and the ability to invest pools of contributions across appropriately varied asset classes. Further, they invest over very long time horizons, so they can

finance large investment projects at competitive rates of return. All of this contributes significantly to economic efficiency by transferring risk to those investors that are best able to bear it.”²⁹

A Societal Perspective

The American Academy of Actuaries has looked at the value of DB plans for employees, employers and society as a whole. While this is written for the US, the same issues are equally applicable in Canada. In reading this, substitute, for 401(k), voluntary DC plans where employees can decide whether or not to contribute. Two important issues are raised here – the importance of the plan assets to the capital markets and the impact on poverty and the social safety net when pension benefits are not adequate.

Here is what they said about society as a whole.³⁰

“Advantages of DB plans vs. DC plans for the nation – There are several advantages, in general of DB plans as compared to DC plans; generally, a higher percentage of an employer’s workforce is covered in a DB plan than in a 401(k) where the employee’s contribution is voluntary; the trillions in DB assets promote national saving, economic efficiency and can reach certain investment markets that 401(k)s cannot; DB plans reduce the nation’s dependence on Social Security and other government assistance programs; and lifetime benefits from DB plans are more likely to help reduce poverty rates for the elderly.”

RECOMMENDATIONS

In this section we set out our recommendations for improving the environment for the DB model. They address the primary causes of the shift away from the model.

Although not organized according to these, our recommendations fall into three basic categories:

- Modernizing Outdated Legislation;
- Strengthening Plans and their Operations; and
- Building for the Future.

RECOMMENDATION 1: Address Dissatisfaction with the DB Model

A major cause of the move away from the DB Model is that plan sponsors (employers) are dissatisfied with the “pension deal.” At the same time, members have concern that the risks that they currently bear are not being recognized in the discussion. We discuss these perspectives below.

RECOMMENDATION 1A: Build a Clear, Certain and Balanced Approach to Risk-Sharing in DB Plans

RECOMMENDATION 1A(i): The Pension Benefits Act (“PBA”) should be amended to provide a clear set of rules for determining the pension deal that achieves balanced risk sharing between plan members and the employer. There should be clarity in the law relating to the funding rules and access to and use of surplus.

RECOMMENDATION 1A(ii): A working group consisting of representation from the Plan Sponsor community, the Bargaining Agent community, the Plan Administrator community and other stakeholders should be established to discuss and make recommendations to the Commissioner with respect to a set of principles for a risk sharing and funding framework acceptable to these stakeholders. In recommendation 14 we return to this recommendation.

Background: There is a strong view held by the DB plan sponsor community that there is asymmetry in terms of the sharing of risk and reward in DB plans. The perception is that plan sponsors bear a disproportionate share of the financial risks relative to employees whereas employees enjoy a disproportionate share of the financial upside relative to employers

The CIA has made proposals to resolve this issue. They state the problem as follows

“Plan sponsors need certainty that when they fund Defined Benefit plans on a more secure basis, they will have access to any surplus funds that may arise when economic conditions are favourable. In the current environment, when economic conditions are unfavourable, plan sponsors must pay more into the pension plan; but when conditions turn favourable, the resulting surplus often belongs to the plan members. This imbalance is perceived by plan sponsors as unfair, and it discourages the secure funding of Defined Benefit pension plans, decreasing the security of members’ pensions, and may contribute to the discontinuation of these plans.”

We make the following observations based on our experience. First, the “asymmetry issue” is the most emotionally charged issue in the pension industry today and divides the Plan Sponsor community and the Bargaining Agent community. When the issue is raised in, as it were, mixed company, the discussion quickly becomes quite polemical. Second, from our perspective, the reality of the risk/reward sharing is more complex and, at least in contributory plans and certainly in public sector DB plans, more balanced than is often portrayed. In contributory plans in which a shortfall arises the employee-side contribution rates can be increased, in some cases significantly, to help fund the shortfall. Many private sector DB plans became non-contributory during the 1980s and 1990s: that is, they stopped requiring employees to make contributions. So when shortfalls arose in those plans, employers could not readily increase employee contribution rates. By contrast, public sector DB plans in Ontario are all contributory with employees making matching or close to matching contributions to those of the employer. Over the last

couple years the employee contribution rates of a number of Ontario public sector plans have been increased to help fund the shortfalls in those plans. A number have also decreased the benefits accrued on future service which is the other way to share some of the risk.

Also, in framing the issue of risk sharing in defined benefit pension plans, it is essential to bear in mind that the unique feature of pension plans as financial instruments is that they are, at root, employment-related benefits. They arise from either an explicit or implicit contract of employment. While they take on aspects of a trust as soon as benefits become vested, they arise from a continuing and continually changing employment agreement. It is impossible to understand the position of employees on questions like risk sharing and surplus sharing without appreciating that fact and without also appreciating that risk sharing can and does occur not just through contribution and benefit levels in the pension plan but also in the broader employment context by adjustments to other parts of the employment terms. For example, a significant increase in contributions to the pension plan by an employer is likely to put pressure on the level of salary increases.

Nevertheless, we are convinced that the “asymmetry issue” is one that must be addressed if the Commission is to fulfill its mandate. We are equally convinced that that is more likely to happen if the plan sponsor community and organized labour come together and develop a set of principles for a risk sharing framework acceptable to both.

Before setting out those principles, we think it appropriate to step back and offer our perspective on the purpose of the regulatory system as it relates to the funding of DB plans. We believe the objective is two-fold:

- first, to ensure that the plan sponsor is being prudent and reasonable in its long-term strategy for funding the plan; and
- second, to protect plan members in the event of insolvency.

The current funding requirements under the PBA reflect a belief that the best way to achieve these objectives is to establish two sets of funding rules, both of which are applied on a relatively short time horizon of three years and to assume that the answer to all questions raised by these rules is to require more funding. In principle, however, the answers to these questions need not be the same. What the regulator should be doing with going concern valuations is ensuring that the assumptions and funding levels are reasonable in the long term, given all of the risks that are faced by the plan, including the credit risk of the plan sponsor. What the regulator should be doing with solvency is ensuring that if the plan were to wind up there would be enough money to pay the benefits. That is to say, solvency really has to do with short-term risk insurance, not long-term funding. This leads to the following:

- The approach to solvency should be risk-based. The solvency requirements should reflect the estimated risk of default and should permit a wide range of possible approaches to the mitigation of that risk.

Additional funding could be one of those risk mitigation strategies, but those strategies could also include third party risk insurance, appropriate security, or some other form of covenant.

- Regulation should set slightly different expectations for plan sponsors, namely, that they:
 - demonstrate that the long-term funding strategy is viable, given the various risks to which the plan is exposed and the opportunities available to it; and
 - disclose and mitigate changes that might materially affect the security of benefits in the event of a forced wind-up.

Under that approach, every three years plan sponsors would have to convince the regulator not that their plan is fully funded, but that their long-term funding strategy is viable under the circumstances. And solvency reviews could be more frequent, depending on the impact of material event disclosures on viability.

Proposed risk-sharing framework: We offer several principles that might be the foundation for a risk-sharing framework: They are as follows:

- The risk sharing method should include ways to provide for sharing of systemic risk such as increases in life span, the impact of inflation, and adverse economic circumstances in a way other than locking the plan sponsor into much higher costs than anticipated. The PBA should accommodate DB plan designs that provide for elements of self adjustment provided that the self adjusting features do not affect accrued benefits and provided the adjustments are made in such a manner that they do not result in shocks to members who are too close to retirement to effectively adjust their retirement plan to accommodate the adjustment. This implies that plan sponsors should be permitted to adjust retirement ages gradually over time. Self-adjusting provisions would be implemented through mechanisms such as:
 - adjusting contributions of both employers and employees (done today in some plans, including Ontario's public sector plans);
 - gradually adjusting retirement ages as employees age; and
 - sharing adverse experience through the plan design

Ideas for risk adjustment can be found in the current plans in the Netherlands and Sweden as described in a paper by John Turner for OPB.³¹

The methods of risk sharing and triggers for adjustment of benefits should be clear and well communicated.

It should be noted that many Ontario public sector plans already have elements of self –adjustment in them or are based on an understanding that

contribution or benefit adjustments might be made in certain downside scenarios so that members bear at least some of the increased cost. In all Ontario public sector plans the cost of the plan is shared because members make regular contributions that match or close to match those made by the employer. The Ontario public sector DB plans could serve as one model for the Commission's consideration.

Other types of plans which have very transparent risk sharing mechanisms could also provide a model. For example, multi-employer pension plans provide that when a shortfall develops the plan must either reduce benefits or increase contributions or some combination of both. One concern that OPB has with multi-employer plans is the ability to retroactively decrease benefits. Any model allowing that should protect members who are approaching retirement as well as pensioners. That reflects OPB's perspective on how collective risk pooling should operate.

- All DB plans should establish and comply with a reserve policy to earmark a certain amount of surplus to enable the plan to withstand a reasonable level of volatility in investments and liabilities.
- Where there is surplus in excess of the reserve amount and an employer has made special payments to discharge a going concern shortfall or solvency deficiency, it should be clear that the employer "owns" an amount of the excess surplus equal to the special payments. This would only apply where, and to the extent that, the Plan Sponsor bears more than 50% of the shortfall through special payments.
- In the event that a Plan Sponsor is required to cover a solvency shortfall there should be flexibility in the method in which the Sponsor chooses to do so provided the method used achieves benefit security. For example, letters of credit or solvency accounts as recommended by the CIA should be considered. Consideration should be given to extending the amortization period for discharging solvency deficiencies.

In August, 2007, the Canadian Institute of Actuaries made a submission to the House of Commons which would modify the requirements for funding of defined benefit plans and strengthen the funding, reduce the volatility of funding, and make the funding requirements applicable to each plan linked to the investments made by the plan. These proposals would also provide a balance between the plan sponsor's assumption of upside and downside risk. The proposals would:

- Permit the use of a Pension Security Trust;
- Establish a Target Solvency Margin;
- Increase the maximum allowable surplus in a pension plan; and
- Mandate adequate funding and encourage funding beyond the minimum level.

OPB supports the direction of these recommendations.

- The CIA recommends that the underfunded pension benefits be accorded the same treatment in bankruptcy as is proposed in Bill C-55 for unpaid current service pension plan contributions. OPB supports that recommendation.
- Consistent with the perspective that the credit risk of the plan sponsor should be a factor in calibrating the solvency requirements applied to a particular plan, OPB believes that many public sector pension plans should be exempt from solvency funding requirements. This would apply to the extent that plan liabilities are guaranteed by the public sector employer.

OPB also believes that the PBA should provide for a range of plan designs. Whether a DB plan or a DC plan or a Hybrid, they should work well in spite of the lack of participant knowledge about retirement planning and investing.

We now move on to the issue of the application of trust law principles to pension plans. That issue, although dealt with separately, is in fact inseparable from, and arises in any discussion of, the risk sharing deal in DB plans. As such, it needs to be addressed in the context of resolving the issues raised in Recommendation 1A.

RECOMMENDATION 1B: The applicability of Trust Law Principles to Pension Plans Should be Reviewed and Clarified

RECOMMENDATION 1B: The application of strict classic trust law principles in the pension context should be reviewed on an issue-by-issue basis. The strict application of classic traditional trust law principles to certain areas of pension law creates difficulties in administration, and has restricted plan sponsor access to/use of excess funds (surplus). In turn, this has created disincentives to the creation and maintenance of DB plans. However, this disincentive must be balanced against the usefulness of trust law for protecting the interests of plan members (e.g., as a protection in the event of employer insolvency). If it is determined that trust law principles should not be applied in relation to a specific issue (e.g., surplus, mergers), specific statutory provision which override common law principles should be enacted where appropriate.

Background: With the Supreme Court of Canada's decision in *Schmidt v. Air Products of Canada Ltd.*, the courts have held that pension plans that are funded through a trust are subject to classic trust law principles (as opposed to contracts or special purpose trusts). Classic trust law principles, however, often do not translate well to the pension plan context, which, in many respects, is essentially a component of the (contractual) employment relationship between employee and employer. For example, prior cases have held that trust law principles may prevent an employer from charging plan administration expenses to a pension fund. This, however, would be contrary to existing trust principles (which allow the trustee to be reimbursed from the fund for administrative expenses), creates an added (and perhaps unnecessary) cost to the sponsor in maintaining

the DB plan, and could prohibit the sponsor from attempting to change the arrangements on a prospective basis, even if the members agree.

Due to the application of classic trust law principles in the pension context, significant complexity and uncertainty currently exists in relation to matters such as surplus withdrawals, plan mergers, contribution holidays and the payment of expenses from a plan. The practical and conceptual difficulties in applying these common law trust rules to modern day pension plans has been recognized by the Supreme Court of Canada in recent pension decisions.

Proposed Approach to Application of Trust Law Principles: An assessment of the advantages and disadvantages of applying trust law principles to the various aspects of pension plan administration should be undertaken on an issue-by-issue basis. Thereafter, if appropriate, amendments to the PBA should be made to override the application of trust law principles on an issue specific basis. This approach is consistent with the Supreme Court of Canada's recent decision in *Buschau v. Rogers Communications Inc.*³² in relation to the application of trust law principles in the pensions context. In this regard, in *Buschau*, the Supreme Court indicated that not all trust law principles are applicable in the pensions context. Rather, an analysis must be made in each case to determine the extent to which trust law principles ought to be applied. An issue-by-issue analysis also recognizes the benefits associated with maintaining the application of classic trust law principles to certain aspects of pension plan administration, while at the same time recognizing that the strict application of classic trust law principles may not be appropriate in relation to other aspects.

In general, this would result in the legislature (not the courts) making pension policy on key issues affecting DB plans, which we believe is the proper result.

RECOMMENDATION 2: Take Steps to Address Perceived Unmanageable Risk

RECOMMENDATION 2A: That the Commission review and consider the application to pension plans of certain of the disciplines developed by the Office of the Superintendent of Financial Institutions (OSFI) to support the ongoing financial strength of federally regulated insurers. The intention of these disciplines would be to encourage the adoption of pension plan management practices to stabilize the cost of the plans to sponsors and members. Benefit improvements and contribution reductions should be subject to special rules and oversight. Regulatory oversight of the funded status of plans should be more proactive in line with OSFI's risk-based oversight of insurers. It would be important that these not impose a significant additional regulatory burden on plan sponsors.

RECOMMENDATION 2B: OPB supports the recommendations of the Canadian Institute of Actuaries that the maximum allowable surplus be the greater of two times the Target Solvency Margin and 25% of the going concern liabilities. When a plan is well funded, contributions should not be shut-off but rather they should be permitted to build up substantial contingency funds.

Background: There is a real perception among employers that DB Plans impose unmanageable financial cost and risk on an employer. The widespread defined benefit plan funding shortfalls that developed during the first half of this decade clearly brought this issue to the fore. But periods of widespread shortfalls occurred in the past and employers stayed with the plans and worked through those periods. Why is the response different this time? We believe it is a combination of all the causes and factors that are identified in this Submission.

The fluctuations in funded status that accompany market swings under traditional pension management approaches are not inevitable. Waring and Siegel point out that better strategies for management are available:

“We are deeply disappointed that there is a pension underfunding crisis. The technology needed to manage pension plans with a minimum of risk and cost has been available, at least in bits and pieces for decades. Little that we have to say is literally new, although we’ve connected the dots and pieces in ways that haven’t been done fully before. Most sponsors, most consultants, and all actuaries simply just didn’t use the technology, even though it was known....”³³

Apart from the risk management techniques identified by Waring and Siegel, we believe there are a number of practices that DB plan administrators can take in managing the funded status of the plan. Using, and funding on the basis of, cautious valuation assumptions, using even more cautious assumptions when costing possible benefit improvements, adopting or recommending to the plan sponsor that it adopt a reserve policy and regularly analyzing and reporting on the systemic funding adequacy of the plan, engaging in ongoing communications with stakeholders about the current and likely future funded status of the plan are a few such practices. In our view, the regulator should have policies directed toward encouraging these practices and monitoring their use by plans. OSFI has such policies with respect to the management of the capital adequacy of federally regulated insurers. Had some of these practices been in diligent use in the 1990s, the benefit improvements and contribution holidays that ultimately proved to be too rich would not have been implemented and many plans would have entered 2001 positioned to weather much better the perfect storm that hit that year. This is certainly the lesson that OPB learned from the experience of the last seven years.

RECOMMENDATION 3: Investigate Methods of Building Incentives for Employers to Balance the Impact of Globalization and Short-termism in the Capital Markets

RECOMMENDATION 3: The Commission should explore and recommend to the Government methods of building financial incentives for employers to sponsor DB plans so as to offset certain macroeconomic factors that are creating a disincentive to do so. These factors include globalization and short-termism in the capital markets combined with increased DB-generated volatility of reported financial results due to changes in Accounting Rules.

Globalization: Business organizations are increasingly global and are facing global competition from businesses operating in jurisdictions where labour costs are low and most employers do not provide DB plans. This has resulted in great pressure to reduce labour costs to remain competitive. On top of this, the capital markets and therefore corporate management have become focused on finance and on short-term market results. This is discussed in the next section. Corporate goals focus heavily on short-term financial performance. The power of the Chief Financial Officer has increased while the focus on responsibility to employees and longer-term talent management has often declined. The system needs to provide an environment that provides stability and some level of cost certainty. Employers need to know their costs.

In addition to our other Recommendations, a pension system or regime that encourages “proper funding” of DB plans will go a long way to bring much greater cost certainty to the employer. Several of the recommendations in this submission should contribute significantly to that end.

Short-termism in the Capital Markets: While there is still much talk about the importance of long-term performance, the reality is that capital markets today focus heavily on companies’ short-term performance. Stock values often rise or fall dramatically and the performance, even competence, of a CEO is often judged based on whether a company misses, meets or exceeds quarterly earnings expectations. This drives private sector managers to place a high value on income statement predictability. Many CEOs wrestle mightily to adopt and hold to a business strategy that they know is right for the company and its shareholders long-term but which involves some short-term pressure on financial results. This should be a serious concern for the long-term health of the broader economy, let alone for the long-term health of the DB model.

Changes in accounting rules, including changes to the accounting for defined benefit pension plans, have increased the volatility of the income statement. Historically, long term pension costs were calculated using smoothing techniques that enabled companies to balance out good years and bad. The downside of smoothing year to year fluctuations was that it could mask a long term decline. In Canada, as elsewhere, smoothing of assets and liabilities has largely been eliminated from financial statements, certainly for pensions as well as for most financial instruments. But, without smoothing, the funded status of defined benefit pension plans is subject to considerable volatility. Both liabilities as well as asset values are subject to volatility and if they move in the opposite direction, as occurred in the early 2000s, the change in funded status can be dramatic and can occur very quickly. So there is a mismatch here: the market emphasis on short-term performance is at odds with the long-term perspective necessary to stay with a defined benefit pension plan through its ups and downs.³⁴ Like most good business strategies, some of the pension structures and funding strategies that produce the best long-term results lead to significantly more year-by-year fluctuation. The fluctuations can be reduced by adopting different plan designs and investment strategies, but often at the price of an increase in long term cost. As a matter of policy, this counter-productive pressure should be recognized and an effort should be made to encourage long-term thinking and action by employers in terms of the retirement income system.

As with the impact of globalization, a system that encourages better pension funding and management of funded status should contribute to greater stability and several of the recommendations made in the submission will make a significant contribution in that regard.

RECOMMENDATION 4: Level the Regulatory Playing Field for DB and DC Plans

We think that simply addressing changes to the DB model, while necessary, will not be sufficient to encourage coverage. The irrational features of the current regulatory system which favour DC plans or no plans at all need to be addressed as well.

RECOMMENDATION 4A: Require DC Plans to Measure and Report to Members Expected Retirement Income Levels and the Adequacy of their DC Assets

RECOMMENDATION 4A: The PBA should be amended to require DC plans to set and disclose to members target lifetime retirement income levels and to monitor and report on the adequacy of assets in the account to fund that level of income so that participants can see what life income is likely to be produced by the account; how it may vary based on various factors including investment returns, expected longevity, inflation and whether the assets are sufficient to fund various levels of benefits. This should apply only if the DC plan is the primary plan provided by an employer. The point here is that primary plans should be focused on retirement and therefore should report to the member on asset/liability management, not solely on asset accumulation. It is recognized that implementing this recommendation may be challenging but the mechanism developed need not be cumbersome.

Background: The regulations to which DB pension plans are subject are designed to regularly monitor and disclose the adequacy of the assets in the plan to deliver on the pension promise. DB plans are established with a view to delivering a target retirement income over the life of the member and the member's spouse. Where the measures applied to DB plans indicate that the assets fall short of the liability for the promised benefit, the regulations force remedial actions to be taken to bring the assets and the liability back into balance. This is all as it should be.

DC plans are not subject to such regulation. They are not required to set and disclose the level of retirement income that might be expected to be generated based on the contributions to the plan and reasonable return and demographic assumptions. There is no ongoing measurement or reporting of whether the assets in the individual's account should be adequate to deliver that expected level of income or what level of income they might reasonably be expected to deliver. There is no remedial action mandated if there is an indication that the assets will not be adequate. In short, they are regulated as savings plans not as pension plans. The primary piece of information that is delivered to members is the lump sum value accrued in the account. These lump sums can seem large to the ordinary person with no information to help in understanding the size of the pool of

capital required to generate a desired level of lifetime income and to address investment, morbidity, longevity and inflation risk. This can contribute to a view of retirement readiness that is out of line with reality. As such, it fails to properly protect members. The differential regulatory burden between the two types of plans is not justified in terms of the need for protection of plan members and it contributes to employer's relative dissatisfaction with the DB model.

RECOMMENDATION 4B: The PBA Should be Amended to Require Some Level of Mandatory Annuitization in Primary Employer-Sponsored DC Plans

RECOMMENDATION 4B: The PBA should be amended to require some level of mandatory annuitization in employer-sponsored DC plans. This would apply only to DC plans that are the primary plan provided by an employer.

The Government should develop an approach to enable the development of a large annuitant pool and a not-for-profit/low cost annuity provider(s).

Background: Longevity is a big risk at an individual level as is investment risk during retirement. It is very expensive to lay off those risks as an individual. These risks are poorly understood by most people. Most concentrate on the possibility of early death and buy life insurance but don't contemplate the possibility of living well into their 90s and the implications of that. Therefore they don't feel a burning need for protection against longevity. The reality is that increasing longevity is one of the reasons for the increased DB plan liabilities that are leading employers to want to lay off pension plan risk. That should tell us that individuals need to be equally, if not more, concerned.

This implies pooling of investment, disability and longevity risks. The DB model offers such pooling of risks and the DC model does not. One of the challenges of providing life income to members of DC plans is the cost of annuities purchased on the open market. There should be a method of providing life income that enables the guarantor of the income to have a reasonable risk pool, and it should be managed efficiently so that expenses can be kept low.

Research shows that even for those with significant net worth, the optimal approach is to annuitize a significant portion of their assets but that most people still do not annuitize.³⁵

This implies that at least part of the benefit should be paid as a life annuity with continued benefits to the survivor. The legal annuity mandate may be set to provide, together with government benefits, a minimum reasonable level of income. Above that, it may be that plan sponsors should be able to choose what they want to set in the way of mandated income.

In the early 1960's, the pension standards legislation³⁶ of the time provided for the creation of an agency to receive, hold and disburse pension benefits. The original thinking behind such an agency was that it would establish an annuity provider so that

members of DB plans who terminated employment and whose benefits were commuted would be able to receive a lifetime benefit at a reasonable cost. The legislation prepared the ground work for establishing a public body such as we recommend, though the agency was never established and the provision was repealed from the PBA on January 1, 1988³⁷.

A public agency that provides annuitization for DC plan members could also be a vehicle to solve the issue of portability of DB benefits in the private sector in Ontario. One of the causes of dissatisfaction with the DB model on the part of both employers and employees in the private sector is the perceived lack of portability of pension benefits. There is a view that the workforce is much more mobile than it has been historically and therefore portability is a more important issue than in the past. While, we question the degree to which mobility has increased, we do think that there should be reasonable portability of accrued DB benefits.

RECOMMENDATION 4C: Address Specific Issues Relating to Insufficient Regulation of DC Plans and Other Retirement Savings Vehicles.

RECOMMENDATION 4C: Address specific issues relating to insufficient regulation of DC plans and other retirement savings vehicles.

Background: As we note elsewhere in this submission, under the current state of the law, it is possible for members of DB plans to elect to convert an accrued DB benefit to a DC account but it is not possible to consolidate an accrued DB benefit into a successor DB pension plan in the context of a divestment. This demonstrates the lack of internal consistency in the regulatory environment. There is a different level of scrutiny that is applied to DB plans that is not applied to DC plans. This makes no sense if one of the primary objectives of the PBA is consumer protection. We support the regulation of DB plans with a view to protecting plan members. However, DC plans pose risks to plan members as well and should be regulated accordingly. That discussion may need to be extended to group RRSPs to level the playing field.

RECOMMENDATION 5 – Take Steps to Increase Appreciation for DB Plans

RECOMMENDATION 5: The Commission should explore and recommend to the Government ways to support education of employees and employers with respect to retirement financial literacy, retirement planning and of the value of employer-sponsored pension plans, including defined benefit plans.

Background: We have developed a lengthy discussion on the lack of employee and employer appreciation of the value to each of them of DB plans and the important role that lack of appreciation is playing in the drift away from the DB model. We have included the full prose in an endnote.³⁸ Here, we summarize it in bullet points.

- For employers, one of the main benefits of sponsoring a DB plan is to help to attract and, particularly, retain top quality talent.

- DB plans are not delivering the expected strong attraction and retention benefit to employers because employees do not understand or appreciate the value of being covered by a DB plan.³⁹ There are several reasons for this, but an historic lack of a concerted effort on the part of employers, plan administrators or the regulator to educate employees is the primary cause.
- On the other hand, the wealth management industry is devoting huge amounts of money, time and effort to promote to consumers the value of DC plans, including RRSPs, tax-sheltered life insurance policies and non-tax assisted savings vehicles. The virtues of investing and controlling one's own assets are extolled, the risks rarely, if ever, mentioned. Several studies have revealed the unrealistic investment return expectations many people hold.⁴⁰
- Nor do employers appreciate the other benefits the DB model can deliver to them. In the ultra-tight labour market employers will face and, indeed, are already facing, the retention feature of DB plans for mid-career employees can be a definite competitive advantage. On the other hand, in an environment without mandatory retirement and in which many, many people are approaching retirement without adequate resources put aside, employers without a DB plan will face a real challenge in retiring unproductive, longer serving employees. Employers also do not understand the potential legal risk associated with sponsoring a DC plan in an increasingly class-action oriented society.
- OPB has made educating the members and participating employers in the Public Service Pension Plan a core strategy. Other Ontario public sector plan administrators such as OMERS are also moving in this direction. The Association of Canadian Pension Management has recently established an education initiative.
- The Government can and should support these initiatives. One way of doing so is by making the encouragement of broad coverage a mandate of the Financial Services Commission of Ontario. Funding education initiatives would be another.

RECOMMENDATION 6: Fix the Inflexible DB to DB Transfer Rules

RECOMMENDATION 6: Sections 80 and 81 of the PBA, which apply to divestments/restructurings, mergers and acquisitions (“divestments”), should be amended to:

1. enable members transferred from one pension plan to another in connection with a divestment to elect to consolidate their pension credit in the pension plan of the transferring employer into the pension plan of the transferee employer;
2. enable the pension plans to enter into transfer agreements which provide for credit and asset transfers that protect the value of the benefit accrued in the transferring plan; and
3. preserve the other rights of affected members currently afforded under Sections 80 and 81.

Background: DB pension plan administrators may enter into pension transfer agreements that enable plan members who change employers outside of a divestment to transfer their pension credit and assets in their former employer’s pension plan (“transferring plan”) to their new employer’s pension plan (“transferee plan”). The regulation under the PBA of these transfers is straightforward and facilitative. There is no requirement for the consent of the Superintendent of Pensions.

By contrast, in the context of divestments, pension plans may not enter into such transfer agreements without the consent of the Superintendent and the Superintendent has interpreted the PBA as precluding the granting of that consent unless the transferee plan provides benefits that are identical to those in the transferring plan. It is rare for plans to provide identical benefits and amending the plans to provide replication is not feasible in most situations. That is particularly so in the case of public sector pension plans. Numerous small divestment situations occur on an ongoing basis in the public service. Moreover, from a human resources perspective it is simply not on to have many different groups of employees doing the same or very similar jobs with different benefits. Even if it were feasible to make such amendments, the resulting requirements to administer various inconsistent benefit structures would be extremely burdensome (and expensive) from an administrative perspective.

Further, in cases involving plan to plan transfers between jurisdictions, the administrator can have a real dilemma if the Superintendent requires adherence to PBA provisions by the new administrator as a condition to approving the transfer, but the other jurisdiction requires the importing plan to determine the members’ benefits (for all service) in accordance with the laws of that jurisdiction (i.e., it applies a “final location” approach to members’ benefit entitlements).

Negative Impact to Members: The inability to transfer assets and liabilities in respect of past service DB benefits in divestment and other situations is inequitable and harmful to affected individuals’ total pension. The inability to transfer assets and liabilities between

DB plans forces members to receive a segmented pension through dual membership in the exporting plan (for past service) and the importing plan (for future service). Members are frequently financially disadvantaged in such case since their final earnings are not applied to consolidated service (because a portion of such service is being held in the plan of a previous employer) and any future ad hoc improvements would not typically apply to all consolidated service.

As noted above, the inability to transfer assets and liabilities in respect of past service DB benefits in divestment and other bulk transfer situations is also inconsistent with PBA provisions in other (substantially similar) member-permitted transfer situations. In other circumstances, the PBA gives members the ability to elect to transfer the value of their pensions (without Superintendent consent) to another pension plan which does not replicate the exporting plan's past service provisions (e.g., portability elections under ss. 42 and 73(2) of the PBA). There is no principled reason why divested members should not have the same ability to consolidate their service.

Potential Solutions: We believe that benefit replication is not the only way to achieve the goal of protecting members' DB accrued pension benefits in divestment/restructuring/bulk transfer scenarios. DB plan-to-plan asset/liability transfers should be permitted in these transactions, on condition that the benefits provided under the importing plan (and accrued under the exporting plan) are of equal value using consistent and appropriate actuarial assumptions.

Furthermore, it is our position that such transfers be permitted on an individual choice basis rather than as a group transfer or bulk transfer. Some members may prefer not to transfer or may not be advantaged by doing so and should not be forced to transfer. That has to be determined on an individual-by-individual basis. In essence, our recommendation is that the protections of Section 80 be preserved for divested members but that they also be provided with the ability to elect to consolidate their past service in the successor plan just as an employee who changes employers outside of a divestment situation would be entitled to do. As long as there is effective communication of the factors that should be taken into account in making the election, there is no valid policy reason to require full replication of benefits.

OPB has advocated strongly for a long time for a solution to this issue. On September 10, 2001, OPB, Hospitals of Ontario Pension Plan (HOOPP) and Ontario Municipal Employees Retirement System (OMERS) provided a detailed Submission to the Honourable James M. Flaherty, Minister of Finance, regarding this plan-to-plan transfer issue. That Submission, which includes a more detailed analysis of the issues identified will be delivered separately to Commission staff.

An Alternative Approach: Grandparenting: Another approach that has been advanced as a solution to this issue is "grandparenting." This involves providing for the affected members to simply remain in, and for the transferee employer to become a participating employer in, the pension plan of the transferring employer. This approach has merit in that it eliminates the adverse impact on affected employees that is caused by the current state of the law. Also it does not require an amendment to the PBA to enable it; the pension transfer agreement approach we recommend does require a PBA amendment.

However, we do not recommend the grandparenting approach for at least two significant reasons. First, it will not be feasible in the private sector. If, as a hypothetical example, the Bank of Nova Scotia (“BNS”) sells an operating unit to the Canadian Imperial Bank of Commerce (“CIBC”), the grandparenting approach would have CIBC as a participating employer in and contributing to the BNS pension plan. That would surely be unacceptable to both. A solution to this issue should be feasible for private sector as well as public sector employers and plans. Second, in either the public or the private sector, the result of grandparenting could be that an employer ends up participating in and contributing to multiple pension plans. That also would be, at best, quite undesirable and more likely unacceptable to most employers. In a context where employers are already trending away from DB plans, an approach that does not meet the needs of employers is not a desirable solution when there is an alternative available that would. That alternative is the pension transfer agreement approach.

We know that the pension transfer agreement approach can be made to work. During 2006 and 2007 the pension transfer agreement approach was implemented for police personnel who are transferred from a municipal police service to the Ontario Provincial Police or *vice versa*. OPP members belong to the Public Service Pension Plan which OPB administers. As such, OPB was an active participant in the development of the approach. The approach followed the recommendations we made above. The transfers were enabled through an amendment to the *Police Services Act* which exempted the transfers from the applicable provisions of Sections 80 and 81. OPB and OMERS have entered into a pension transfer agreement and are in the course of processing the transfers.

OPB has had an opportunity to review the submissions to the Commission on this matter of the Ministry of Government Services (the Plan Sponsor) and of the Association of Administrative and Professional Crown Employees of Ontario (the largest Bargaining Agent representing members of the Plan). Those submissions are excellent and OPB fully supports them. We have also had the opportunity to review the submission of the Association of Law Officers of the Crown which addresses many of the items we raise in this Submission. It too is an excellent submission and OPB fully supports it.

RECOMMENDATION 7: Develop a Multiple Employer DB Platform that Would Facilitate Participation by Small Private Sector Employers

RECOMMENDATION 7: OPB recommends that:

1. a multiple employer DB platform be developed that would provide good opportunities for small private sector employers to participate in a DB plan;
2. the platform should be based on the Ontario multiple-employer public sector model; and
3. a working group, consisting of private sector employers, private sector labour organizations, public sector employers, public sector plan administrators and public sector bargaining agents be established to develop the platform.

Background: Collectively, small businesses are a major employer in Ontario. A robust pension system should enable small employers to provide DB pension plans to their employees.

Very small DB plans lack economies of scale and are prohibitively expensive. Moreover, the size at which it is feasible to maintain a DB plan has increased over the last ten to fifteen years. The environment in which defined benefit plans operate has changed significantly during that period and these changes have dramatically increased the sophistication required to manage a plan to acceptable standards. On the investment side of plans, the emergence of private equity, hedge funds, derivatives and infrastructure investments are cases in point. Most in the industry believe that it is, and will be going forward, necessary for a plan to include at least some of these in its portfolio if it is to generate the returns necessary to fund the plan at reasonable contribution rates. To succeed in these asset classes requires a high degree of expertise and access to the best investment managers.

The standards for pension governance have also become much higher in recent years. In many respects of course this is to be applauded. However, the development, implementation and maintenance of governance excellence require resources and expertise. As an organization that has dramatically improved its governance over the last several years, we can attest directly both to the value of improved governance and to the additional resources and expertise required to do so.

The same can be said of the regulatory and legal environment. One need only read the recent report of the Financial Services Commission in the OMERS/Borealis Capital matter to gain a perspective on the expectations of the regulator for defined benefit plan administrators. Several judicial decisions have also made the waters much more challenging for plan sponsors and administrators to navigate (e.g. the decisions in the *Monsanto*, *Transamerica* and *Stairs* cases⁴¹).

Together these developments have created an additional burden on both sponsors and administrators of defined benefit plans and have contributed to employers deciding not to establish new DB plans and to close existing plans. OPB believes that, for larger plans, the return from increased investment opportunities and better governance has more than compensated for the increased burden. For smaller plans, that may not be the case. This implies that economies of scale are needed to manage plans well.

A Basis for a Solution: The Ontario Multiple-Employer Public Sector Model: There are actually many small employers in the public sector as well and these employers have operations that are every bit as varied as in the private sector. The Ontario public sector has developed a model that accommodates those smaller employers very successfully. These plans have several characteristics in common:

- Administration by independent special purpose agencies, plan administrators rather than plan sponsors bear some the fiduciary and operational risk.
- Good economies of scale and professional staffs.

- Administrators governed by capable Trustees/Boards focused exclusively on pension administration often with representation of different stakeholders.
- Cover employees of a number employers including small governmental agencies
- Defined Benefit plan designs with good benefits.
- Contributory and therefore employers share risk with members.
- Strong commitment to plan participants.
- Longevity, investment and disability risks are fully pooled.
- Spousal survivor benefits are provided.

Encouraging the development of a similar multiple employer model for the private sector could be the key to ensuring broader coverage by enabling small and mid-sized employers to participate in DB plans. The Ontario public sector model could be translated into a model for broader regional or industry plan administrators or cooperatives. This establishment of such platforms in the private sector would also be beneficial to large employers.

RECOMMENDATION 8: Take Steps to Bolster both the Actual and Perceived Security of the DB Pension Promise

RECOMMENDATION 8: OPB recommends that the Pension Benefits Guarantee Fund be continued. Steps should be taken to ensure that it remains strong, well managed and well funded and the insured benefit levels are updated to reflect current income levels.

The purpose of this recommendation is to address cost certainty as well as benefit security. Addressing the risk sharing arrangement as recommended earlier will result in more secure funding of DB Plans. However, a strong and secure PBGF accomplishes two important things: it provides pension plan members with an added sense of security with respect to accrued benefits and it is an appropriate approach in light of our recommendation that the risk sharing deal be clarified.

Background:

Over the last seven years in Canada and the US, there have been a small number of high profile failures by DB plans to keep the pension promise, particularly in troubled industries such as the steel industry and the airline industry. Also much has been said in the media about the potential for such failures in the auto manufacturing sector as the Big 3 North American auto manufacturers have faced particularly difficult times. The widespread funding shortfalls that developed in the early 2000s have understandably further undermined the perception of the protective value of DB plans in the minds of employees. Combined with other factors discussed in this submission this has contributed to a desire of employees to have their assets segregated and to have control over those assets.

Employees must be given an accurate picture of the security of the DB pension promise. The fact is that these failures are rare exceptions. The vast majority of DB plans have delivered, and will continue to deliver, the promised benefits. Unfortunately, there has been no strong voice outside of individual plan administrators conveying that counterbalancing message to employees. In our view, this would be a proper role for a regulator and for a DB industry association. As discussed elsewhere in this submission the regulator does not, but in our view should, have a mandate to promote coverage by employer-sponsored plans, including DB plans. There is no DB-dedicated industry association in Canada. The Association of Canadian Pension Management does promote the DB model but is somewhat divided and therefore limited in its effectiveness because it is a pan-industry association. Its mandate includes the promotion of other models such as the DC model and a significant portion of its membership is interested in promoting the DC model. Our earlier recommendations regarding the education of employees about the value of the pension plans, and particularly the DB model, should include discussion of the security of the pension promise.

Many of the recommendations that we have made in this submission would contribute significantly to pension plans fully delivering on the pension promise through good times and bad. Reforms to the system will need to be well communicated to the public to overcome the sense among some that there is a high risk that DB plans will not deliver on their promise.

OPB does believe that a safety net is essential for that small number of instances of insolvency and therefore recommends continuance of the Pension Benefit Guarantee Fund. We also believe that maintaining the Fund to protect members against insolvency is appropriate in view of our recommendation that the risk sharing arrangement between members and employers be clarified.

RECOMMENDATION 9: Provide FSCO with a Legislative Mandate to Encourage Broad Coverage by Employer-Sponsored Plans

RECOMMENDATION 9: The PBA should be amended to include a mandate for FSCO to encourage broad coverage of employer-sponsored pension plans, including defined benefit plans.

Background: In the face of a decline in DB coverage, it would be desirable for the regulator of pensions to have stepped forward to address the causes of this trend with a view to encouraging coverage. That has not happened because the Financial Services Commission of Ontario has no legislative mandate to encourage coverage. That, in our view, is unacceptable. FSCO has an essential role to play in bringing the stakeholders together to develop solutions to problems with the PBA that are contributing to the decline in coverage. FSCO also has an essential role to play in ensuring that the public has the proper perspective on the security of the pension promise. We strongly recommend that such a mandate be given to FSCO immediately.

In fact, until 1997, promoting the establishment and improvement of pension plans throughout Ontario was part of the former Pension Commission of Ontario's mandate under section 96 of the PBA. This mandate was repealed at that time when an Act to establish the Financial Services Commission of Ontario was introduced. Under the Pension Benefits Act, R.S.O. 1990 C.P.8, section 96 read as follows:

96. *It is the duty of the Commission,*
- (a) to administer this Act and the regulations;*
 - (b) to promote the establishment, extension and improvement of pension plans throughout Ontario;*
 - (c) to advise the Minister in respect of the business of the Commission; and*
 - (d) to make recommendations to the Minister in respect of Pension Plans.*

It is our recommendation that the duty of FSCO to promote the establishment, extension and improvement of pension plans, and particularly DB plans, throughout Ontario be added back into the PBA.

RECOMMENDATION 10: Remove all Unnecessary Complexity and Cost of Administration of DB Plans

There are several key areas where the PBA, as interpreted by the courts, creates unnecessary complexity, cost and uncertainty in the administration of defined benefit plans.

RECOMMENDATION 10A: Remove Unnecessary Constraints Under the Current Investment Rules

RECOMMENDATION 10A: The PBA should be amended to remove certain prescribed quantitative investment restrictions that impose unnecessary constraints or have become outdated and are no longer practical.

Background: Very generally, ss. 22(1) of the PBA imposes the so-called “prudent person rule” which requires pension plan administrators to exercise the care, diligence and skill that a person of ordinary prudence would exercise in dealing with the property of another person in the investment of pension plan assets. This requirement serves as a guiding principle for all investment related decisions. OPB supports the prudent person approach as the appropriate guiding principle for the investment of pension plan assets.

In addition, as in most Canadian jurisdictions, the PBA requires pension plan investments to comply with sections 6-7.2 and Schedule III of the Pension Benefits Standards Regulations, 1985 (the “Federal Investment Rules”). The Federal Investment Rules contain various quantitative limits and restrictions on related party transactions.

Problems with Certain Investment Rules: OPB believes that some of the quantitative limits under the PBA have become outdated. An example of one such rule is the “30%

Limit”. The 30% Limit prohibits plan administrators from investing plan assets in the securities of a corporation to which are attached more than 30% of the votes that may be cast to elect the directors of the corporation.

The 30% Limit was implemented at a time when pension funds were largely passive investors that were much smaller in size than they are now, relative to the economy as a whole. With the growth in size of public sector plans and the switch to more active (private equity) investment strategies, the 30% Limit has become problematic for the following reasons:

- Complex and costly structures are required in order to ensure regulatory compliance.
- These complex and costly structures act as a further disincentive to potential investment partners, or as a reason for such partners to exact a “price” for their tolerance of such structures.
- Due to the 30% Limit pension plans may be forced to take a sub-optimal proportion of desirable investment opportunities.

Nature of Review: We’re of the view that the Federal Investment Rules need to be reviewed, and requirements which impose unnecessary constraints and have become outdated should be removed. In their absence pension plan administrators should continue to be subject to the overriding general “prudent person rule”. For example, in respect of the 30% Limit, even if such limit is removed, a pension plan administrator considering an investment in securities to which are attached more than 30% of the votes that may be cast to elect the directors of the corporation will need to consider whether such investment is prudent in the circumstances.

RECOMMENDATION 10B: Amend the Rules for the Division of Defined Benefit Pensions on Marriage Breakdown Rules Require Reform

RECOMMENDATION 10B: The current provisions in the PBA relating to the division of DB pensions on marriage breakdown should be reviewed and revised with the objectives being:

1. finality/ certainty of outcome at the time of division;
2. enabling the spouse who is not the member of the plan to elect to keep his or her share of the benefit in the plan;
3. cost-neutrality to the plan;
4. low cost to implement for both the member and spouse and for the plan administrator; and
5. clarity for members as to the amount/value of their benefits.

Background: A robust and sustainable pension system should recognize that the benefits earned must protect not just the employee but also dependent family members, most often a spouse.

The *Family Law Act* (the “FLA”) is the primary statute setting out rules governing the division of property on marriage breakdown in Ontario. The PBA then imposes additional rules that relate specifically to registered pension plans. The current FLA and PBA regime governing the division of pension benefits is extremely complex. Further, the application and interpretation of this complex regime by the Courts has not been consistent. As a result, pension divisions can be very time consuming and costly to administer for all parties involved (members, non-member spouses and plan administrators). As well, the lack of clarity in the legislation puts pension plan administrators at risk of a claim that the pension benefits were improperly paid out. Below we highlight some examples of the difficulties with the current PBA regime.

Survivor Benefits When the Marriage Breakdown Occurs Prior to Retirement: One aspect of the PBA requiring clarification is whether or not a survivor benefit can be payable to a member’s former spouse in the event that the member dies after pension commencement in circumstances where the couple separated prior to the member’s retirement. On its face, section 44 of the PBA indicates that post-retirement death benefits are not payable to a member’s former spouse in such case. However, arguments can be made based on the Ontario Court of Appeal’s decision in *Ontario Teachers’ Pension Plan Board v. Ontario (Superintendent of Financial Services)*⁴² that a member can effect a form of assignment prior to retirement such that post-retirement survivor benefits are payable to the non-member spouse if the member dies after retirement. In OPB’s view, as the assignment of pre-retirement death benefits is expressly permitted pursuant to s. 48(13) of the PBA, the assignment of post-retirement death benefits should be expressly permitted as well. It is inequitable that the timing of the member’s death determines whether or not the member’s former spouse ultimately receives a survivor benefit from the plan.

The 50% Rule : Subsection 51(2) of the PBA provides that a member’s spouse cannot receive more than 50% of the pension benefits accrued during the period the parties were spouses. OPB views this provision as a public policy principle that no more than 50% of a member’s pension should be payable to his/her spouse in marriage breakdown situations. However, there have been cases where 100% of a member’s pension was payable to the non-member spouse: 50% was assigned to the spouse as an equalization payment under the FLA and the other 50% was assigned to the spouse for support.⁴³ OPB is opposed to such “stacking” as it views it to be contrary to good public policy and to the intention of the PBA.⁴⁴ The general rule under the PBA is that pension plans are exempt from seizure and assignment. This reflects a strong policy position that recognizes that DB pension plans are protective and an important element of the retirement security for members and their spouses. Division of pensions on marriage breakdown and using the pension as a source of support payments is a justifiable exception to the general rule. However, that exception should be limited to 50% of the pension as is the intention reflected in the PBA. Marriage breakdown invariably involves a diminishment of the standard of living of both parties. It is in the interests of

spouses and of society at large that the protective element not be entirely removed from the member spouse. This issue should be clearly addressed in any reform measures.

Recommended Reform: As a matter of public policy, married couples should divide pension benefits at the time of the marriage breakdown. It is essential, and a matter of significant public interest, that spouses be able to settle their affairs and divide one spouse's pension with certainty of outcome, clarity, low cost and fairness to both spouses at the time of the marriage breakdown.

OPB would support a "division scheme" implemented at the time of marriage breakdown pursuant to which the non-member spouse effectively becomes a form of plan member entitled to a lifetime benefit from the plan in which the member participates (equal to the value of the portion of the pension assigned to the non-member spouse).

While an immediate division of the pension through a lump sum payment to the non-member spouse would be the simplest solution to these challenges, OPB opposes any approach which would force a non-member spouse to receive a lump sum payment instead of a pension benefit. In our view, forcing a non-member spouse to accept a lump sum payment is generally less valuable than allowing the non-member spouse to become entitled to a continuing pension payment. Risk has a price and if the non-member spouse is forced out of the DB plan that spouse's risk is increased. OPB would be amenable to an approach which provides the non-member spouse with the option to elect either a lump sum payment or a pension benefit.

OPB has advocated for a legislative solution to this issue for some time. A copy of OPB's submission to the Ministry of Finance and Ministry of the Attorney General regarding this matter will be delivered separately to Commission staff.

RECOMMENDATION 11: The Roles of All Industry Stakeholders Should be Clarified

RECOMMENDATION 11: OPB is of the view that the specific roles, duties and responsibilities of all parties involved in the establishment, maintenance and administration of a pension plan should be clarified. In this regard, the PBA should clearly specify which roles, duties and responsibilities are subject to a standard of care under the PBA. Plan Administrators: OPB believes that DB plan administrators should be subject to an express duty of care to take reasonable steps to protect the long-term health of the plan. OPB believes that advisors to plan administrators should be subject to a similar duty in providing services to plan administrators. It should be made clear that the duty of care owed by advisors is both to the plan administrator and the plan beneficiaries. A code of ethical conduct should be developed and applicable to advisors to plan administrators. Among other things, the code should address the potential conflict of interest where actuaries provide services relating to the pension plan to both the plan sponsor and the plan administrator.

Background: Currently, the PBA recognizes a number of parties who are involved in the ongoing investment, operation and administration of a pension plan: the administrator, the employer, the actuary, the pension fund trustee/custodian and the auditor. Under the

current model, the primary (and over-arching) legal responsibility for most functions associated with the administration and investment of the plan rests with the administrator.

In relation to private sectors plans, the employer acts as both “administrator” and “sponsor”, but owes different obligations to members in each role. Pursuant to s. 22 of the PBA an employer acting as administrator owes fiduciary duties to members and must accordingly act in the best interests of members and beneficiaries when carrying out administrator functions. However, case-law has established that, when acting in a plan sponsor capacity, an employer may act in its own interests (i.e., the interests of its respective shareholder(s)), rather than in the best interest of the members and beneficiaries of the plans.⁴⁵ This distinction is more clearly demonstrated in the public sector context than in the private sector context as in the public sector context the role of administrator and sponsor are separated.

In addition to pension plan administrators, fiduciary duties are imposed on “agents” of an administrator pursuant to ss. 22(8) of the PBA. However, “agent” is not defined under the PBA and, as discussed below, the circumstances in which fiduciary duties apply to service providers are not sufficiently clear.

Duties and Responsibilities of Third Parties Recognized by the PBA: The precise duties and responsibilities of third parties such as the plan actuary, fund trustee/custodian and the auditor should be more clearly defined under the PBA. Importantly, the PBA should clarify whether actuaries, fund trustees/custodians and auditors are “agents” for purposes of s. 22 of the PBA and therefore subject to fiduciary duties. (Of course, alternatively, a concept other than “agent” could be used under the PBA.)

In the case of actuaries, the application of fiduciary duties can significantly impact the manner in which their functions under the PBA are carried out. In this regard, when preparing valuation reports there are a range of acceptable methods and assumptions that meet acceptable actuarial practice. If the actuary is subject to fiduciary duties, arguably, the actuary would be obligated to adopt the more conservative methods and assumptions that result in increased contributions to the pension plan as opposed to those that result in the minimal contributions. Actuaries’ obligations in this regard require clarification. Are the actuaries simply advisors to the plan sponsors, and owe their legal duties only to the sponsors, or do they play a “watchdog” role on behalf of plan members (similar to that played by auditors) and owe duties directly to plan members?

Additional Third Parties Involved in Plan Administration: The Canadian pension industry has evolved: in addition to the actuary, fund trustee/custodian and auditor there are now also an array of consultants, third party plan administrators, software providers and others who assist “administrators” with their day-to-day plan administration duties. The scope of services provided by these third parties varies. In some cases, employers (*qua* administrators) fully outsource all plan administration duties to a third party administrator. In other cases, the third party service providers assist with specific discrete functions (e.g., programming of benefit calculation software). However, in any particular situation, it is not clear whether a particular third party service provider is an “agent” for purposes of ss. 22(8) of the PBA. Accordingly, the specific roles, duties and responsibilities of such third parties is not clear and should be clarified (including

clarification of the fiduciary duties, if any, owed to members directly by such third party service providers).

Moreover, if such third parties are indeed agents for purposes of the PBA, it is common for them to insist on a limitation of liability clause in their contract with the administrator. How should such limitation of liability provisions be treated? Recent amendments to the *Supplemental Pension Plans Act* (Quebec) provide that such limitation of liability clauses are void. If such a result is intended for Ontario plans, the PBA should be amended to clarify the liability of any “agents” of the administrator and any permissible limits thereon.

RECOMMENDATION 12: Financial Advisors Providing Services to a Client who is a Member of an Employer-sponsored Plan Should be Regulated

RECOMMENDATION 12: Financial Advisors who provide services to a client who is a member of an employer-sponsored plan should be regulated. In particular, Financial Advisors who counsel DB or DC plan members with respect to the withdrawal of assets from their plan should be subject to legislatively imposed obligations to fully disclose and inform their clients about the risks of withdrawing their assets from the plan. Consideration should also be given to making it clear that advisors are fiduciaries to their clients in connection with such advice.

Background: When members cash the value of their benefit out of a DB plan, investment and longevity risk, and in some cases inflation risk, are being transferred onto the member. Financial and investment advisors often have a personal vested interest in advising pension plan members to transfer their benefits out of the pension plan to an individual arrangement (e.g., to increase the amount of assets under their management, and the fees generated by such assets). In the past, some public sector plans have encountered problems with financial and investment advisors enticing members to transfer their accrued DB pension benefits to individual arrangements (e.g., by building up the member’s expectation as to possible future returns on investment), which was ultimately to the members’ detriment when the individual arrangements did not perform as projected.⁴⁷

OPB is concerned that many financial/investment advisors appear to be operating under little or no rules or regulatory supervision in luring members out of DB plan with promises of greater returns. They are in a conflict of interest situation with great power over their vulnerable clients – the classic circumstances for the imposition of fiduciary duties.

Also, OPB is concerned that if portability rights under the PBA are expanded, many members may exercise such rights (on the advice of their financial and/or investment advisor), yet, for the reasons outlined above, such transfers are often not in the best interest of members.

RECOMMENDATION 13: The Current Locking-in and Commutation/Transfer Rules Should Be Maintained

RECOMMENDATION 13: The current locking-in and transfer rules under the PBA should be maintained.

Background: OPB strongly supports legislation which helps ensure that pension benefits, which are crucial to individuals' retirement savings, are not prematurely depleted due to unlocking of benefits and/or improperly diverted to individual arrangements by the transfer of benefits out of DB or DC pension plans.

The data referred to in this submission demonstrates that where lump sums are paid out, many people will have problems at higher ages.

It takes steady saving at reasonable levels over a working lifetime to generate an adequate retirement income. Capital withdrawals during working years negates years of disciplined saving, subject the individual to a high risk of poverty during retirement and should be strongly discouraged and, except in exceptional circumstances, prohibited. OPB believes that Ontario's locking-in rules have sufficient flexibility to allow for capital withdrawals in exceptional circumstances and strongly opposes any change to the locking-in rules.

The Importance of Locking-in Rules: Under the current PBA regime, benefits are locked-in after two years of plan membership, except in limited circumstances (as discussed below). Locking-in serves to ensure that benefits accrued under a registered pension plan are used as retirement income. To this end, OPB strongly opposes any further erosion of the current locking-in rules. The current exceptions to the locking-in rules, which permit unlocking only in circumstances of small amounts, shortened life expectancy and financial hardship, provide flexibility to pension plan members in appropriate circumstances.

Locking-in helps ensure pension plan members have the financial means to enjoy a comfortable and dignified retirement. As well, it helps alleviate the burden on the means-tested public old age security system. Such practical benefits of locking-in far outweigh the philosophical objections of some critics (who take the position that locking-in rules are paternalistic). Locking-in is consistent with the fundamental purpose of a pension plan – to provide retirement income.

Eliminating the locking-in rules (or further eroding them) will change the fundamental nature of the DB and DC plans from a “retirement savings plan” to that of a “tax deferred savings scheme”.

The Importance of Limits on Commutation/Transfer of Cash Value of Pensions: As well, OPB supports the current PBA regime which does not require that commutation/cashing out be offered to members who are entitled to an immediate pension from a plan.

Portability under s. 42 of the PBA effectively allows a member to convert his/her accrued DB benefits into a lump sum DC amount (the commuted value). Due to the assumptions and methodology used to prepare the commuted value calculation, the lump sum commuted value is often less valuable to members than ongoing DB payments from a pension plan. After the conversion occurs, the lump sum value of the member's accrued DB benefits become vulnerable to market fluctuations. A member's pension benefits can be significantly reduced due to market losses. In contrast, when a member remains entitled to DB benefits payable from a plan, these benefits are not subject to market fluctuations. Allowing individuals who are entitled to an immediate pension (and are therefore close to retirement) to cash out could also have the effect of enticing members to make a bet on their future mortality and/or ability to generate investment returns that will out perform the value of their DB benefit. The point behind the provision is to protect members from ill-advised risk when their human capital is spent and they therefore have little ability to absorb the risk.

RECOMMENDATION 14: A Working Group Consisting of Plan Sponsors and Bargaining Agents Should be Created to Develop Solutions to Current Issues that Would Support the DB model

RECOMMENDATION 14: A process should be established to bring representatives of the Plan Sponsor community and Bargaining Agents as well as the Plan Administrator community and other stakeholders together to discuss and develop solutions to encourage defined benefit coverage. We recommend that the Commissioner be appointed to lead and facilitate this initiative.

Background: It is clear that many of the areas for reform identified in this submission will engage the sensitivities of the plan sponsor community and of employees/bargaining agents/professional associations. Plan Sponsors and Bargaining Agents have divergent views both in terms of identifying the key challenges facing the DB model and as to the solutions to the problems. There have been some attempts to come together to develop solutions acceptable to both but with little or no success. This makes legislating a solution a high risk endeavour for any government and as such little in the way of legislative reform has occurred.

We believe that it is possible for these groups to come together. At the risk of sounding naïve, both have much common ground that they could work on. As an organization at the interface between a Plan Sponsor and several Bargaining Agents that represent members of the Public Service Pension Plan, we see what can be done if we all work together. There are a number examples of this in the context of the PSPP. For example, as noted above, this year the Plan Sponsor, the Ontario Provincial Police Association, the Police Association of Ontario, OMERS and OPB worked cooperatively to develop a

ground-breaking solution to the long-standing issue of the inability of divested police personnel to consolidate their pension credit in one pension plan. Four years ago, the Plan Sponsor, the Association of Management, Administrative and Professional Crown Employees of Ontario (“AMAPCEO”) and OPB worked together cooperatively to develop an approach to improve the governance of OPB with excellent results. Those improvements have benefited all the beneficiaries and other stakeholders of the Plan.

We believe that, if the recommendations ultimately made by the Commission are generally supported by the Plan Sponsor community and Bargaining Agents, the likelihood that they will be implemented will increase significantly. That level of support is unlikely to develop unless there is a specific initiative to bring the groups together.

CONCLUSION

The foregoing are our submissions, respectfully made, to the Commission.

¹ The trend away from DB Model to the DC model in the private sector across the world is well documented. In a report prepared by Watson Wyatt for OPB (*Public Sector Pension Plan Design Trends Abroad*, submitted in letter dated 10 February 2006 to Mark J. Fuller (see Appendix A, Section D of description of private sector for each country and Appendix C for Canada)) the magnitude of the shift is clearly presented. This letter will be delivered separately to Commission staff.

United Kingdom

In the United Kingdom, about 85% of public sector workers and 20% of private sector workers are covered by employer sponsored DB pension plans, 10% of private sector workers are in occupational DC plans and below 10% are in group personal pensions. About 75% of private sector DB plans are now closed to new entrants. A minority of DB plans have also been closed to future accrual and some have been wound up (terminated). Replacement plans are generally DC plans with lower benefits. (*Public Sector Pension Plan Design Trends Abroad*, submitted in letter dated 10 February 2006 to Mark J. Fuller from Watson Wyatt, citing *The First Report of the Pensions Commission*, October, 2004, page 62.) This letter will be delivered separately to Commission staff.

Canada

In Canada, about 10% to 20% of DB plans have been changed to DC for future hires in recent years. The pace of change seems to have accelerated from mid-2006 to date. (*Public Sector Pension Plan Design Trends Abroad*, submitted in letter dated 10 February 2006 to Mark J. Fuller from Watson Wyatt, Question 14). This letter will be delivered separately to Commission staff.

The percentage of Canadian workers earning from \$30,000 to \$40,000 covered by DB plans dropped from 40% in 1996 to 34% in 2004. More than half had no plan. At the \$80,000 annual earnings range, the percentage covered by DB plans dropped from 49% in 1996 to 43% in 2004. At the \$80,000 earnings level, the percentage covered by DC plans increased from 5.84% to 8.29%, and the percentage with no plan increased from 44% to 47%. (Canadian Institute of Actuaries and University of Waterloo, *Planning for Retirement, Are Canadians Saving Enough?* June 2007, page 8, table 8).

The percentage contributing to an RRSP at the \$30,000 - \$40,000 level dropped from 46% in 1996 to 43% in 2004. At the \$80,000 level, the percentage dropped from 81% to 77%. (Canadian Institute of Actuaries and University of Waterloo, *Planning for Retirement, Are Canadians Saving Enough?* June 2007, page 8, table 9).

² C.D. Howe Commentary, No. 250, *Ill-Defined Benefits, The Uncertain Present and Brighter Future of Employee Pensions in Canada*, June 2007.

³ Turner, John, *Pension Policy Around the World: Australia, the Netherlands, Sweden, and Provident Funds in Asia*, paper prepared for the OPB, July 2007. A copy of this Paper will be delivered separately to Commission staff.

⁴ John Hancock Financial Services, *Eighth Defined Contribution Plan Survey: Insight Into Participation, Investment Knowledge & Behavior*, 2002.

⁵ Canadian Institute of Actuaries and University of Waterloo, *Planning for Retirement, Are Canadians Saving Enough?* June 2007.

⁷ Hacker, Jacob S., *The Great Risk Shift* (Oxford, 2006, Preface, page x).

⁸ See *Rational Decumulation*, David F. Babbel, Wharton School of the University of Pennsylvania, Draft: May 22, 2006 www.fic.wharton.upenn.edu/fic/papers/06/0614.pdf

⁹ Mitchell, Olivia S., Utkus, Stephen P., *Pension Design and Structure: New Lessons from Behavioral Finance* (Oxford, 2004).

¹⁰ Canadian Institute of Actuaries, *Seeing Beyond Risk: Submission by the Canadian Institute of Actuaries Presented to the House of Commons Standing Committee on Finance*, August 2007.

¹¹ We recognize that it is difficult if not impossible to actually add up the increased costs. But risk pricing theory certainly supports this conclusion.

¹² See *Rational Decumulation*, David F. Babbel, Wharton School of the University of Pennsylvania, Draft: May 22, 2006 www.fic.wharton.upenn.edu/fic/papers/06/0614.pdf

¹³ A recent Pew Study, *Working After Retirement: The Gap Between Expectations and Reality* shows very different results – with only 12% of retired people working for pay now. The Pew study records both a retired and semi-retired category. In the last study 23% of the total participants were retired and 2% were semi-retired.

Morbidity and disability continue to be an important reason for people to leave the labour force. The United States Congressional Budget Office (CBO) has looked at the early exit of some Baby Boomers from the Labour Force (CBO, *Disability and Retirement: The Early Exit of the Baby Boomers from the Labour Force*, November 2004). The CBO has examined the Survey of Income and Program Participation (SIPP) database to look at people who were aged 50-61 and not participating in the labour force in 2001. Status was based on self reporting, and people were classified as retired or disabled. Some of their key findings included:

- Men and women not in the labour force because of disability generally had much lower income, higher poverty rates, and fewer assets than those who were retired.
- Of the total population aged 50-61, 14 percent of men and 24 percent of women were reported as not being in the labour force at any time during the year. Of the men in the study, 32 percent were retired, 64 percent were disabled and 4 percent reported the reason for not being in the labour force as other. Among the women, 26 percent were retired, 40 percent were disabled and 34 percent reported as other the reason for not being in the labour force.

There would, of course, be a much larger number of people who have left the workforce for health reasons that do not reach the level of a disability.

¹⁴ A number of factors come together to create unanswered questions about how long people will work and what they often say. Key points are:

- More than seven in ten workers say they expect to retire gradually or work as part of their retirement. While many people want to work in retirement, they may be seeking different job options and working conditions other than regular full-time work.
- About four in ten retire earlier than planned.
- Of people age 50-61, who are not in the labour force, many more are disabled than retired.
- Typical workers say they expect to retire at 65 but are more likely to retire at 62 (Center for Retirement Research, Data Profile #4, 5 April 2006).
- More people say they plan to work in retirement than actually do work in retirement.

Society of Actuaries Key Findings and Issues: Phased Retirement and Planning for the Unexpected, 2005 Risks and Process of Retirement Survey Report, April 2006.

¹⁵ Society of Actuaries, *Key Findings and Issues: Phased Retirement and Planning for the Unexpected, 2005 Risks and Process of Retirement Survey Report*, April 2006).

¹⁶ Ambachtsheer, K., *The Pension Revolution*, (Wiley, 2007).

¹⁷ Ambachtsheer, K., *The Pension Revolution* (Wiley, 2007).

¹⁸ Society of Actuaries and LIMRA, *Spending and Investing in Retirement: Is There a Strategy?*, 2006.

¹⁹ SEI Investments Canada, 18 May 2004, press release.

²⁰ His discussion, condensed somewhat, (on page 71) is as follows:

“Human Foibles

The fact is that most people are not very good at solving the retirement savings problem on their own. People have difficulty keeping track of too many moving parts. Even rational experts have difficulty estimating their actual pattern of lifetime savings, asset returns, taxes, longevity, and then deriving the optimal savings rate and investment policy from these projections. In addition, beyond these complex computational challenges lie important behavioral issues. These are:

1. **Lack of self-control.** Many people rationally understand the need to save for retirement, but are incapable of following through on their intention. So they constantly overconsume today and undersave for tomorrow.
2. **Lack of firm preferences.** Research shows that many people will answer the same question differently, depending on how it is asked. For example, enrollment in voluntary DC plans is much higher if employees are automatically enrolled with the choice to opt out than if they have to make a positive election to opt-in.
3. **Inertia and procrastination.** People tend to follow the path of least resistance in their decision making. For example, after investment education seminars, a high proportion of participants say they are going to change their fund and asset allocations, but only a small proportion actually do.
4. **Choice overload.** Research says that there is a negative relationship between the number of investment choices offered in DC plans and the plan participation rate.
5. **Improper inferences and/or overconfidence.** People tend to see patterns in random data or simply rely on readily available data rather than the right data. For example, fund or asset mix shifts are often made based on just a few years of good or bad historical results.
6. **Loss aversion.** Faced with the realization of a certain loss, many people will double up in an attempt to recoup their investment. This aversion to realizing losses may explain why life annuities are so unpopular with many DC participants: they may die early and lose their bet with the insurer.”

²¹ Mitchell, Olivia S., Utkus, Stephen P., *Pension Design and Structure: New Lessons from Behavioral Finance* (Oxford, 2004).

²² Society of Actuaries, LIMRA and Mathew Greenwald & Associates, *Public Misperceptions About Retirement Security*, 2005.

²³ Council of Institutional Investors Primer on DB Plans, www.cii.org/defined_benefits/index.htm.

²⁴ Additional Studies:

How have defined benefit plans performed vs. the individual investor?

Median 17 year return (through December 31, 2000) = 13.1%

Average individual investor return for same period = 5.2%

(Source: Committee on Investment of Employee Benefit Plan Assets (CIEBA), *The U.S. Pension Crisis: Evaluation and Analysis of Emerging Defined Benefit Pension Issues*, March 2004, page 11 — CIEBA cites two sources for this data – Mellon Pension Trust Universe and Dalbar study)

The following is some additional data from the U.S. cited in Waring, M. Barton and Siegel, Laurence B., *Don't Kill the Golden Goose* (Barclays Global Investors and the Ford Foundation, May 2006):

“Economist Alicia Munnell estimates that between 1985-2001 DB plans outperformed DC plans by .8 percent on average.” (page 5)

“Research on advisory fees by Profs Freeman and Brown indicated that DB plans pay only about half of what DC plans for investment advisory services, .28 percent versus .56 percent of assets.” (page 6)

“The Investment Company Institute, which represents the mutual fund industry, found that the total operating expense ratio of DB plans was on average 40 bp less than that of mutual funds, 31 pb for DB versus 71 bp for DC. And, those numbers understate DC costs by excluding 12-b1 marketing and distribution fees that average between .25 and 1.00 percent of assets.” (page 7)

“Research indicates that very small DB plans pay proportionately higher administrative costs than either larger DB plans or DC plans. The smallest plans (15 employees) have expenses of 3.1 percent of payroll for DB versus 1.44 percent for DC. But for large firms (10,000 employees) the costs are nearly the same for DB and DC and they are quite small – .23 percent for DB versus .16 percent for DC.” (page 6-7)

(Sources: The Council of Institutional Investors paper, *Protecting the Nest Egg: A Primer on Defined Benefit and Defined Contribution Retirement Plans*, cites the data above, no publication date, location – Washington, DC)

“In 2000, the State of Nebraska reviewed its two DC retirement plans for state and county workers and found that between 1983 and 1999 the DC plans’ investment returns averaged only 6 percent compared with 11 percent for the state’s DB plans.” (page 7)

“On average, investment returns from DC plans are lower than for DB plans, resulting in significantly lower investment earnings over an individual’s lifetime. According to Boston College economist Alicia Munnell, DB plans outperformed DC plans by one percentage point annually, on average from 1988 to 2004. For a person contributing \$5,000 to a DC plan each year for 40 years, the difference between an 8.0 percent annual return and a 7.0 percent annual return amount to a loss of over \$279,000. Other studies show that individual, non-professional investors may underperform the market by as much as 2.0 percent annually. The difference between an 8.0 percent annual return and a 6.0 percent annual return amounts to a loss of over \$521,000.” (page 11)

“Administration and investment costs for DC plans can be more than four times higher than for DB plans. In DC plans, these costs are borne directly by individual plan participants through deductions from their DC accounts. According to the Investment Management Institute, the operating expense ratio for DB plans averaged 31 basis points in 2003 (31 cents per \$100 of assets) compared with 96 to 175 basis points for DC plans.” (page 11)

Source: NCPERS Research Series, *The Top Ten Advantages of Maintaining Defined Benefit Plans*, May 2007, Washington, DC.

²⁵ Waring, M. Barton and Siegel, Laurence B., *Don't Kill the Golden Goose* (Barclays Global Investors and the Ford Foundation, May 2004, page 4).

²⁶ Fidelity Retirement Index – “Fidelity Calls for Urgent Action to Spare a Generation of Workers with Defined Contribution Pensions from a Retirement in Poverty”, May, 2006

www.fidelityinstitutional.com/assets/documents/press%20release.doc; *Threat of Two Tier UK Pensions*, BBC News, May 10, 2006, <http://news.bbc.co.uk/1/business/4757255.stm>)

²⁷ *Corporate Commitment to Pension Provision*, Fidelity International, January 2007.

²⁸ World Bank website, *Policy Issues in Private Annuity Markets*, July 4-5, Insurance Committee OECD, <http://rru.worldbank.org/>

²⁹ Cited in National Round Table on the Environment and the Economy, *Sustainable Pension Plans*, 27 July 2007. <http://www.nrtee-trnee.ca/eng/publications/capital-markets/pension-plans-capital-markets-eng.html>)

³⁰ American Academy of Actuaries, *The Value of Defined Benefit Plans, Executive Summary*, Washington, DC 20901, undated.

³¹ Turner, John, *Pension Policy Around the World: Australia, the Netherlands, Sweden, and Provident Funds in Asia*, paper prepared for the OPB, July 2007.

³² [2006] 1 S.C.R. 973 (“*Buschau*”)

³³ Waring, M. Barton and Siegel, Laurence B., *Don’t Kill the Golden Goose* (Barclays Global Investors and the Ford Foundation, May 2006).

³⁴ In 2005 OPB eliminated the use of asset smoothing in plan valuations, but that decision was made in the context of the Public Service Pension Plan. It does not reflect a belief that it is either necessary or desirable for other plans, their members and pensioners or their sponsors to do so.

³⁵ See *Rational Decumulation*, David F. Babbel, Wharton School of the University of Pennsylvania, Draft: May 22, 2006 www.fic.wharton.upenn.edu/fic/papers/06/0614.pdf

³⁶ *An Act to Provide for the Extension, Improvement, and Solvency of Pension Plans and for the Portability of Pension Benefits*, S.O. 1962-63, c.103 section 13.

³⁷ *An Act to Revise the Pension Benefits Act*, R.S.O. 1987, c. 35.

³⁸ *Lack of Appreciation of DB Plans*

Lack of Employee Appreciation

It is important to remember that pension plans form part of an employer’s human resources strategy and, more particularly, the employer’s total compensation strategy. One of the main benefits an employer hopes to gain from sponsoring a DB plan is attraction and retention of top talent. If it does not realize that benefit, one of the main incentives to sponsor the plan is gone and there will be little to offset the perception that there is only downside risk in sponsoring a DB plan. In order for that benefit to be realized employees and prospective employees must fully appreciate the value of the DB plan. The fact is, they do not. There has been surprisingly little employee resistance to the closure of DB plans. This suggests that employees attach very little value to DB plans relative to DC plans or individual retirement savings accounts. It also suggests that they do not understand the risk that has been shifted onto them.

Appreciation cannot happen without a deep understanding of the plan and that level of understanding can only happen if there is effective and ongoing education and communication of the benefits and value of the plan. The defined benefit industry has simply not spent much time, money or effort in communicating and keeping in front of employees the incredible value of a good DB plan. Why is that? First, of all, historically employees did not insist on being educated. In fact, in our experience, until recently employees were actively disinterested in having their pension plan explained to them, at least until they were on the

eve of retirement. Second, we believe that employers did not feel the need to do so. The ready availability of labour meant that it was not essential that employers maximize the attraction retention value of their plan. In addition, DB plans are protective: the plan sponsor and the collective membership of the plan assume certain risks so that the individual employee is protected from them. The protective nature of the plan probably led employers to take the attitude that they did not have to educate employees. The view was that employees did not really need to know much about the plan because they did not have to manage it and their retirement was “looked after” by the plan and that was all they really needed to know.

Moreover, to properly explain the value of a DB plan requires both an explanation of the pension benefits that the plan provides which are complex enough but also an explanation of the risks that the employee is being protected against. The latter involves the explanation of an interactive matrix of risks including investment risk (both during employment and during retirement), longevity risk, morbidity risk, job loss and employability risk and inflation risk. As set forth earlier, research has shown that people are insufficiently educated to properly assess the value of protection against longevity risk. There is no doubt that educating employees to properly understand these risks is a formidable challenge. However, the wealth management industry is today spending huge amounts of money to promote the value of the DC model, including DC plans, RRSPs, tax sheltered life insurance policies and private non-tax-assisted savings. Based on our experience, substantial effort has been directed at comparing the return and value that their products offer favourably to defined benefit plans. The virtues of controlling and investing one’s own retirement funds are extolled; the risks rarely, if ever, mentioned. This has been enabled by the longest period of strongly rising equity, bond and real estate markets in history over the last 20 to 30 years, which, we believe, has led to the development of an unrealistic perception of both return and risk at the individual investor level. No wonder then, since appreciation of value is often comparative, that employees might not value their defined benefit plans.

If the appreciation deficit is to be corrected there needs to be a concerted effort by all participants in the industry, Employers, Plan Administrators, the Regulator and Advisors to DB Plans, to demystify DB Plans with plain language communications and also to explain how a DB plan can make an extremely valuable contribution to a sound financial retirement plan. The wealth management industry understands this and is acting on it. It is moving to providing not just investment management services but strategic wealth management advice to the mass affluent and even to those with relatively low net worth. The wealth management industry has no incentive to properly evaluate and explain to customers the value of a DB plan. In fact, the financial structure of the wealth management industry rewards asset-gathering and so, for most in the industry, creates an incentive to work against DB plans. Moreover, under the current state of the law, wealth management advisors are not fiduciaries.

It would be unrealistic to expect private sector employers for whom the pension plan is not their core business to dedicate the resources, money and effort to develop effective approaches and tools to fully educate employees about DB plans. One might have expected the sponsors or administrators of the large public sector plans to identify and take on this challenge but, to date, that has not happened to any significant extent. There are signs that is changing. In 2005, OPB made educating plan members on the value of their plan a core strategy and we will be partnering with the sponsor of the plan which also intends to step up its efforts in that regard. Other public sector plan administrators such as OMERS and HOOPP also appear to be taking up this effort. One might also have expected plan sponsors and administrators to come together to cause an industry association to do so. Again, until recently, that has not happened. It is very encouraging that the Association of Canadian Pension Management has recently established an Education Initiative working group of the Strategic Communication Committee to identify ways in which financial literacy, particularly around retirement income plans and retirement savings can be improved. The Committee is expected to review partnering opportunities with government, boards of education, as well as with plan sponsors and labour groups to develop and implement its strategic plan. The Committee is expected to have a recommendation by early summer of 2008.

Lack of Employer Appreciation

There is also a lack of appreciation of the value of DB plans to employers. The value or lack thereof of DB plans is being assessed through the rear view mirror. In our view, employers who look through the windshield will come to a different conclusion as to their value and those who choose to go with a DB model plan will find that they have a competitive advantage.

DB plans exert a very strong retention effect on mid-career to late-career employees. Looking backward, the value of that effect has not been high over the last 20 to 30 years because there has been an abundance of labour. Employers do not have a great deal of experience with a broad based, prolonged, tight labour market. With the tight labour market that is already emerging and that will tighten much further as the demographic trends play out in the labour market, this benefit of DB plans will be increasingly valuable to employers. Failure to understand to date the combined impact of the elimination of mandatory retirement and the removal of a DB plan.

On the other hand, employers are failing to factor in the impact of the elimination of mandatory retirement and connecting the dots on the importance that will place on assisting their employees to prepare financial for their retirement. The fact that most employees are not saving adequately for retirement will mean that more employees than ever will need to continue to work past age 65. Some of those employees will be unproductive. In the absence of a DB plan, in light of the elimination of mandatory retirement, employers will face a formidable challenge in easing those employees into retirement. Those who cannot do so may find that the elimination of mandatory retirement is a material drag on their productivity and management of their labour costs.

Employers also fail to understand fully the potential risks associated with sponsoring a DC model plan. Employees who reach retirement without adequate funds will be looking for someone to blame and for a source of funds to improve their finances. Sponsors of DC plans will be targets. There is already sign of increasing litigation in the US relating to DC plans.

³⁹ OPB member survey results. Also, see Jonathan Forman, Alfred P. Murrah Professor of Law, University of Oklahoma and Vice Chair of the Oklahoma Public Employees Retirement System in a presentation to Canada Cup of Investment Conference, June, 2007, Toronto, Ontario. A copy of Professor Forman's paper will be delivered separately to Commission staff.

⁴⁰ John Hancock Financial Services, *Eighth Defined Contribution Plan Survey: Insight Into Participation, Investment Knowledge & Behavior*, 2002.

⁴¹ *Monsanto Canada Inc. v. Ontario (Superintendent of Financial Services)* [2004] SCC 54 (S.C.C.).

Aegon Canada Inc. v. ING Canada Inc., 2003 CarswellOnt 4879 (Ont. C.A.).

Ontario Teachers' Pension Plan Board v. Ontario (Superintendent of Financial Services) 2004 CarswellOnt 526 (Ont. C.A.).

⁴² (2004) 70 O.R. (3d) 61 (C.A.).

⁴³ See e.g., *Nicholas v. Nicholas* (1998), 37 R.F.L. (4th) 13 (Ont. Gen. Div.) and *Kennedy v. Sinclair*, [2001] O.J. No. 1837 (Fam. Ct.)

⁴⁴ There have also been cases that criticized the notion that a court can assign one half of the member's pension for equalization payments and one half of the member's pension for support purposes for the reason that it may constitute what is known as "double dipping". "Double dipping" is a term used to describe a situation in which, upon marriage breakdown, a member's pension is taken into account as a capital asset when calculating the equalization payment owing, and then taken into account again when the pension is in pay as an income stream, for purposes of determining the member's obligation to provide spousal support. In this regard, the Supreme Court of Canada in *Boston v. Boston*, [2001] S.C.R. 413

indicated that “double dipping” is generally to be avoided, although it may be permissible in certain circumstances.

⁴⁵ *Re Imperial Oil Ltd. Retirement Plan (No. 2)* (August, 1995), 18 C.C.B. 198 (Ontario Pension Commission).

⁴⁷ James Daw, “Pension Fund Strategy a Risky Business”, *Toronto Star*, 26 April 2007 and “*Join against pension ruling, victims urged; Court decision could be devastating for retirees setting up a business*”, *Toronto Star*, 4 September 2007.