Bell Pensioners' Group Inc.

Improving the Defined Benefit Pension Plan Model: Issues, Proposals and Benefits

June 2008

Overview

The following recommendations are presented for the consideration of the

Nova Scotia Pension Review Panel

1. Recognize defined benefit pension plan retirees as key pension plan stakeholders and consult with them during the development of revisions to pension legislation and regulations.
2. Provide pensioners with better access to current information and data regarding the well-being of their pension plans.
3. Mandate full solvency funding of pension plans at all times thus solving a number of outstanding issues to the benefit of all pension plan stakeholders.
4. Provide for pension indexation (cost of living adjustments).
5. Legislate independent reviews of pension plan governance and administration and ensure the regulator is adequately funded.
6. Resolve surplus ownership issues.
7. Call for an assessment of the adequacy of current pension levels given the growing trend of eliminating sponsor paid post-retirement benefits.

1. Introduction

The Bell Pensioners' Group (BPG) has been actively advocating the need to improve the defined benefit pension plan (DB plan) model and related legislation for several years. It therefore welcomes the decision by the Nova Scotia Government to review pension benefits legislation.

The Bell Pensioners' Group is:

- A registered not for profit organization that advocates on behalf of the more than 30,000 retirees of Bell Canada, almost one-third of whom are paying members.
- It encompasses retired company officers, executives, management, non-management, engineers and other professionals, clerical employees and technicians.
- It is part of a growing network of pensioner groups - the Canadian Federation of Pensioners - that together represent 100,000 retired individuals from across Canada.

The main DB plan issues are the same everywhere in Canada, regardless of which government jurisdiction is responsible for the legislation. Over the last two years, BPG has prepared several papers[1] on DB plan issues in which we have made major proposals on how to resolve them. BPG believes its proposals, once fully implemented, will result in an enhanced DB plan model that benefits ***all*** stakeholders.

When a DB plan is forced to wind-up with a solvency deficiency it is the pensioners who stand to lose the most. They not only lose what for many is their primary source of post-employment income, they are most likely unable to replace that lost income. This loss of spending power can lead to pressures on the local and provincial economies and on government agencies which provide social assistance to the elderly.

Pensioners, too often in the past, did not have a voice or did not demand one at the discussion tables when it came to updating pension legislation and regulations. But economic and financial events of the past number of years have been a wake-up call to pensioners to band together and collectively present their views. As current DB plans mature, the number of pensioners is increasing to the point where they can outnumber the active members.

Pensioners must be actively consulted during the ongoing efforts to update pension plan legislation and regulations.

[1] See page 7 for more information on accessing these briefs online

2. Keep Pensioners Better Informed

A prime concern for pensioners is the difficulty encountered in obtaining current information on the financial status of their pension plan. Many existing pension plan legislation and regulations across Canada leave much to be desired in mandating that plan administrators adequately inform retirees about their plan in a timely and consistent manner. A lack of information about the security of an individual's major source of retirement income during times of financial and economic uncertainty inevitably leads to growing levels of stress and fear amongst the retiree population.

Given today's ever more quickly changing business and economic climates and given modern information and systems technologies, it is unfathomable that pension administrators are allowed up to 6 months in order to file annual financial returns on pension plans and 12 months in which to file a triennial or more frequent actuarial evaluations.

Current Nova Scotia legislation does not specifically provide for *the right of all retirees to have access to all the information they need to assess the financial health of their pension plan*. And what they and all employees <u>and the regulator</u> also need now is *more timely access* to this information.

Information technology now exists for pension plan data to be prepared and disseminated much more quickly and economically than when the current pension legislation and regulations were enacted. Receiving pension plan data sooner would benefit the regulator as well as all pensioners.

One way in which this can be achieved for retirees is by providing online access through the internet to a website where they can find:

- The full text of the plan;
- Significant amendments to the plan;
- Copies of all the financial, actuarial and other reports to be posted in the same timeframes as when these are submitted to the regulator; and
- Allowing pensioners, without internet access, the ability to receive this same information from the plan administrator, upon request, in hard copy form.

3. Eliminate Pension Plan Deficits

There is a distinct correlation between deficit funding of pension funds and the myriad of problems and issues identified in the Nova Scotia Pension Review Panel's discussion paper as well as in consultations conducted by other jurisdictions.

3.1 Full Solvency Funding

There are numerous benefits which would derive from requiring a pension plan to be fully solvent at all times. *These include:*

- Long term financial security for pensioners;
- Easier movement or transfers of employees between plans;

- Facilitates the planning and implementation of plan amendments;
- Reduction in regulatory workload;
- Elimination of the need for unforeseen special funding by the sponsor in the case of solvency deficiencies (see *The Pension Reserve Fund* section below) which impact on the cash flow and can threaten the financial well-being of a sponsor's own business; and
- Reduction in number of pension plans being wound-up with funding deficits.

Given recent financial and economic realities, the current practice of allowing funding deficiencies to exist for a number of years in the normal course of events is totally unacceptable. Sponsors' businesses are becoming increasingly exposed to global competition and to rapid changes in their business cycles. Starting in the early 2000's there was ample evidence of DB plans developing significant solvency funding deficits very quickly as a result of sharply falling interest rates and low rates of return on investments. New criteria for calculating solvency funding for pension plans in recent years exacerbate the problem and increase the risk of funding deficiencies.

One way to solve this problem is to provide the means for the sponsor to create and have access to a reserve fund – within the pension plan arrangement itself – in order to ensure that the pension plan is fully solvent at all times.

3.2 The Pension Plan Reserve Fund

The current DB plan model allows for a measure of overfunding, commonly referred to as a 'surplus'. The amount of overfunding is currently set by the Income Tax Act which assumes the current limitations are adequate for every DB plan. The recent rash of DB plan solvency deficits indicates that these arbitrary funding limitations are inadequate.

BPG endorses the Canadian Federation of Pensioners proposal to modify the DB plan model to include a reserve fund as contained in its June 2008 submission to the Nova Scotia Pension Review Panel. A reserve fund would be established for each DB plan to assist in ensuring that the plan would always be solvent.

The DB plan's actuaries would determine the minimum level of reserve funding to protect against adverse deviation. The actuaries would also determine a maximum funding level taking into account the known or more predictable factors applicable for that particular plan sponsor to ensure that the plan is always fully solvent. For example, a sponsor whose business is subject to a recurring and steep business cycle would be allowed to have a larger reserve fund than a sponsor who has a relatively flat business cycle.

In this way, the reserve fund is tailored to help the sponsor meet solvency funding requirements without having to cope with unplanned or unforeseen demand on the working capital of its business, especially during periods of economic slowdown, high interest rates and/or low rates of return on the plan's assets..

The actuarial profession would have to set the standards for reserve funding in association with regulators and the Canada Revenue Agency. Once this has been decided, there would be no further need for the Income Tax Act to stipulate specific DB plan funding limits.

4. Indexation of Pensions (Cost of Living Adjustments)

Pensioners are retiring earlier and living longer. This means that their pension has to provide them with adequate spending power for many more years than was the case in the past. But the longer retirees are living on fixed incomes, the more exposure they have to the effects of economic inflation on their spending power. The Old Age Security and the CPP/QPP plans recognize this by providing cost of living adjustments or indexation on a regular basis.

Current occupational pension plan legislation allows for DB plans to provide for indexation. Some sponsors have provided for automatic indexation within their DB plans; others have indicated they would index pensions with funding from their business profits when they saw fit to do so; while many others have taken no action whatsoever. That being said, it is a reality that between the time when current pension legislation was implemented and now, the Bank of Canada has made significant progress in controlling inflation and as such it is now easier for pension plan sponsors to afford and fund pension indexation.

BPG strongly urges an amendment to current pension legislation to require every plan to include a provision for indexation on an annual basis. *BPG further recommends that the Pension Review Panel undertake to study whether or not full indexation of DB plan pensions is feasible or if annual indexation should be capped in order to protect the financial integrity of the plans.*

5. Provide for Independent Review of Pension Plans

Currently annual DB plan financial reporting is subject to review by accounting auditors. There is no requirement for any other aspect of pension plan administration, including governance, to be reviewed by independent professionals. Considering what is at stake for all pension plan stakeholders, ***independent assessment of the pension plan administration would benefit all concerned.***

- It would ensure that standards set out in legislation and regulations and by professional organizations, such as the Canadian Institute of Actuaries, are being followed.
- It would serve as a check on the influence of the sponsor who is also the employer or the party that engages the plan administrators.
- It would provide greater assurance to retirees and the capital markets that there is proper governance and administration.

In addition, ***the pension plan regulator requires the mandate and funding to enable it to conduct its own reviews***, particularly if a plan seems to be experiencing funding difficulties or its administration appears weak. It would be preferable to pensioners to have the regulator step in to offer timely guidance, warnings or take more drastic action, for example, before a pension funding issue becomes a pension plan wind-up issue.

6. Resolve the Surplus Ownership Issue

It has been widely reported that pension plan sponsors are concerned with recent court rulings affecting or potentially affecting their ability to have full access to pension plan surpluses. It does seem that there is a case of asymmetry to be made here, especially for plans with single sponsors and whose employees do not contribute directly. Until this is resolved, there is every possibility that sponsors will be reluctant to fund their DB plans by more that the minimum required. This is to no one's benefit and needs to be resolved quickly.

Under the proposal to establish a reserve fund, both the Canadian Federation of Pensioners and BPG have stated that whoever contributes to the reserve fund will have the right to request access to any overfunding, subject to approval by the regulator and the Canada Revenue Agency. This would eliminate any question of ownership on a going forward basis.

If a pension plan is in a surplus position prior to new legislation for a reserve fund, additional or temporary regulations may be required to ensure, where the pension plan text is not explicit regarding all aspects of surplus ownership, that agreement must be reached (with arbitration if necessary) between all parties on this matter within a specified period of time. To leave it unresolved is only to leave it open to dispute at any time in the future.

7. Some Thoughts on Pension Benefit Guarantee Funds

Barring a large unforeseen catastrophic event DB plans *maintained on a fully solvent basis*, as outlined above, will never be in a wind-up position where a case could be made for Nova Scotia needing a Pension Benefit Guarantee Fund (PBGF) similar to the one in Ontario.

The United States of America equivalent of a PBGF is consistently under-funded and has in the past required large government provided financial bail-outs. The Ontario PBGF also has had and continues to have its own financial difficulties.

Another weakness with the Ontario PBGF is that the financial assistance provisions established over 20 years ago for subsidizing pensions have not been kept current with changes in the cost of living.

8. Review the Implications of the Erosion of Employer Provided Post-Retirement Benefits

There are many employers either considering or who have recently taken action to limit, or eliminate altogether, post-retirement benefits for future retirees. There have also been some employers trying or threatening to do the same with current retirees.

When employers decide to sponsor a DB plan, they likely will take into consideration that the level of pension to be paid includes due consideration for the value of employer subsidized post-retirement benefits paid outside of the pension plan. BPG is unaware of any studies done to determine if employers who subsequently decide to eliminate post-retirement benefits have taken this factor into consideration and adjusted the pension levels accordingly.

If the level of pension being paid has not changed, then the retiree will have to use more of his pension income to pay for medical and dental expenses previously paid for by the employer. This could have a dramatic impact on retirees' standard of living.

A study is required to determine the current as well as to predict the future impacts on retirees and on the government's social safety net as a result of employers' decisions to eliminate post retirement benefits. With the aging demographics for Nova Scotia and for the country, revisions to public policy may be required to address this situation.

THE FOLLOWING DOCUMENTS ARE ACCESSIBLE AT

www.bellpensionersgroup.ca/bpg/pension_reform.htm

- *BPG Response* to the May 2005 Finance Canada consultation paper, 'Strengthening the Legislative and Regulatory Framework for Defined Benefit Pension Plans Registered under the Pension Benefits Standards Act, 1985', September 2005 (also posted on the Finance Canada website).

- *Improving the Defined Benefit Pension Plan, Making a Good Thing Better*, BPG, January 2007.

- Discussion paper on *Requiring Continuous Full Solvency and a Reserve Fund for each Private Defined Benefit Pension Plan*, BPG, March 2007.

BPG has also submitted briefs to the:
- Ontario Expert Commission on Pensions; and
- Alberta-British Columbia Joint Expert Panel on Pension Standards

The briefs are accessible on their respective websites.

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This brief was prepared by the BPG pension committee. Members of the committee volunteer their time and have developed an in-depth understanding of DB pension plans issues learned through continuous study, attendance at professional seminars and conferences, and through the constant monitoring of relevant media and pension stakeholders' websites.

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