Submission to the Nova Scotia Pension Review Panel

By

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(United Steelworkers)

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The United Steelworkers represent over 280,000 workers across Canada in virtually every industrial sector. Our membership includes not only steelworkers, mine and smelter workers but also workers in universities, light manufacturing, retail, banking, health care and private security industries. Our concerns about recommendations made by this Panel extend beyond the impact on those of our members who will be directly affected in Nova Scotia. The potential role that the Panels recommendation may have in setting standards means that the impact of these recommendations could be repeated in pension jurisdictions across the country.

Our union welcomes the opportunity to submit our views on many of the issues that have been raised in the review panel's discussion paper which outlines the panel's broad mandate "to recognize current legislative standards and review improvements that will allow pensions to work for both employers and employees". Your paper raises twenty-six questions dealing with thirteen different subject matters and yet the expert panel has only allowed less than five weeks for stake holders to develop and submit a comprehensive response to the issues raised.

In our view the time period provided by the panel is not adequate and we would urge you to extend the submission deadline to January 2009 which would provide seven months for stakeholders to fully respond to the issues at hand. I would also note that this time frame would be similar to those provided during similar pension legislation reviews elsewhere in Canada.

In an effort to meet the current July 4 deadline we are making this submission as an attempt to address some of the issues the expert panel has raised. If the deadline for submissions is extended we may provide a revised submission in the future.

The issues in context

No consideration of issues in pension regulation is meaningful unless the issues are examined in the context of the Canadian retirement income system, the objectives of that system and the role of private pensions in it.

Canada’s retirement income system consists of five key elements:

- the Old Age Security and Guaranteed Income Supplement, both of which are universal Federal programs subject to either direct or indirect income testing;
- the Canada Pension Plan, an earnings related employment pension plan which is universally applicable to employment income up to a maximum income amount;
- tax assisted retirement saving provided through private pension plans and so-called “group RRSPs” established through contracts of employment;
- tax assisted individual retirement savings through RRSPs; and
- non tax-assisted private savings.

The fundamental goal is to provide for adequate retirement incomes for all Canadians, hence the widely stated objectives of adequacy and coverage.

The system was deliberately designed to reserve a significant role for privately determined, tax-assisted and employment related retirement arrangements and for individual, tax-assisted retirement saving. In particular, both universal public pensions (OAS and GIS) and the public employment-related pension plan (the CPP) were restricted so as to leave “room” in the system for private arrangements.

Private retirement savings arrangements play a significant role in Canada's retirement income system. As a matter of public policy, we are counting on private savings and privately determined retirement savings vehicles to provide a significant proportion of the income of Canadians in retirement. As individuals, working Canadians are counting on employment-related retirement savings (both direct savings and foregone earnings) for a significant proportion of their incomes in retirement.

Pension regulation arises from the need to support and oversee the important public policy role of private retirement savings arrangements. It is also founded upon the need to protect the rights of individual pension plan members. The need for individual protection arises from two key facts of life about pensions:

- There is a substantial imbalance of information, power and control between beneficiaries and employers / plan sponsors; and

- Because retirement income rights are deferred rights, individual interests may only become apparent when they crystallize at retirement, when it is generally too late to address prior problems.

Of course, plan beneficiaries are not the only stakeholders in the private retirement income system. Plan sponsors and employer contributors to "group RRSPs" generally provide at least half of the financial resources necessary to fund these arrangements. These costs are a substantial cost of doing business. But it is clear that the regulatory system exists in its current form because of the need to protect the rights of plan members and beneficiaries.

The elements of the pension regulatory system cannot be evaluated without understanding: 1) what rights are being protected; 2) how these rights have changed over time; and 3) the public policy objectives of pension regulation.

In the earliest days of private pensions, employers provided pensions on an ex gratia basis. There were no beneficiary rights. Pension payments were essentially a gift to former employees. They were not given to every employee, and they could be suspended or eliminated at the employer's discretion. Employers could, and did, pick and choose among employees at the time of retirement and could, and did, suspend pension payments to retirees who, for example, were relatives of union "agitators".

The first step in the evolution of pension rights was to recognize that, once a former employee has retired and begins to receive a pension, he or she had a right to continued pension benefits on terms at least as favorable as those in place at retirement. Employers could not discriminate among employees in determining eligibility for pension at retirement or suspend payments after retirement.

The regulations encoding these rudimentary rights were contained in income tax regulations and their role protecting individual rights was ancillary to their role in protecting the public purse.

The second step coincided with the introduction of the first pension benefits acts in the mid-1960s. In the first Nova Scotia Pension Benefits Act in 1977 the concept of "vesting" was introduced into the regulatory system. By introducing vesting and locking-in for employees aged 45 or more with ten or more years of service, the NSPBA in 1977 recognized that plan member had rights that crystallized before retirement.

The third and fourth steps in the evolution of pension rights developed separately in the courts and in the national pension law reform exercise that led to major legislative changes in Nova Scotia in 1988. The courts determined that beneficiary rights arise from principles of trust law rather than of contract law. Thus, mere participation in a pension plan could crystallize certain rights including the right to share in the distribution of surplus assets. In other words, member rights "accrued" from the beginning of plan participation even where the plan was a "non-contributory" plan.

By limiting the waiting period for plan participation, introducing mandatory two-year vesting, requiring that at least half of the value of a pension benefit must be attributable to employer contributions, grow in rights, and mandating portability on termination before retirement. The 1988 changes established the principles in Nova Scotia law that pension rights accrue throughout an employee's period of employment and that they should be recognized at the earliest reasonable time and crystallize when the employee ceases to be an active participant in the plan.

The 1988 reforms reflected the evolution of recognized private pension rights to that point. While not perfect they were small steps in the advance of pension plan member rights. The United Steelworkers will not be able to support any proposal that would diminish any rights that currently exist under Nova Scotia legislation. In fact we hope this review panel will work towards improving those rights.

Review Panel Objectives

The stated objective of the Review Panel's consultation paper is to seek the views of Nova Scotians on how to strengthen this framework in order to improve the security of pension plan benefits and ensure the viability defined pension plans.

The vast majority of our members are provided pension coverage under flat rate plans and so we are concerned about the security, viability and sustainability of these plans in particular and all registered plans in general.

A word on security

The retirement benefits from employer-sponsored defined benefit plans can and do make up a significant portion of a worker's retirement income. Unionized workers negotiate these benefits through collective bargaining while they are still employed, but the benefits they negotiate affect the income they will rely upon for their standard of living in the future. Workers only receive these benefits upon leaving their employment and therefore upon leaving the bargaining unit from which they negotiated those benefits. Therefore, the security of benefits is of particular importance to workers. No worker wants to see the pension that they counted on change or disappear after they have left the position from which they had the most bargaining power to influence their pension entitlement.

A word on viability

Pension plans involve a commitment today to on-going payments in the future. These arrangements exist over the long-term. It is in the interest of workers to know that the pensions are regulated in such a way that ensures they remain viable over the long-term. For workers, this means that plans should be carefully managed and monitored. We are well aware, however for

many of the parties interested in this consultation, viability means making pensions cheaper.

We are concerned, that for many stakeholders, the debate's starting point precludes a scenario in which security is guaranteed without reducing today's costs. As workers, we believe that the security is something already owed to us, and not something to be granted provided we enter into a trade-off that sheds some of the pension cost.

The issues for discussion in this consultation, for the most part, centre on viability, coverage, funding and allocating funding surpluses and not the actual benefit levels. But changes in the framework that place inherent value in reducing the sponsor's short-term costs will inevitably put pressure to place value on reducing long-term costs as well. We are concerned that we may be heading down a path in which the assumed mutual objective necessarily includes reducing the costs of pensions generally. The question of how to ensure this kind of viability begs a particular answer. The only way to really reduce the overall cost of pensions in the end is to reduce benefits. We want to be cautious that ensuring viability isn't reducible to eroding retiree benefits and minimizing plans sponsors funding obligations.

Viability must mean sustainability

Too often the Steelworkers have found themselves in defensive battles to maintain defined pension benefits from the desire of employers to cut costs generally. Our pension plans should not become the sponge that absorbs the employer's other financial problems. Workers should not be asked to sacrifice a portion of their retirement income in order to balance the employer's books today, especially if the imbalance is a result of factors external to pensions. So while we are thankful to be part of this consultative process, we recognize from the very beginning that we as unionized workers and future retirees have much to lose or gain depending on what we take viability to mean.

The Steelworkers are willing to work towards solutions that ensure pension viability where this means that they are sustainable. It does not mean simply, or in all cases, that they are more affordable. When viability means sustainability, the priority is first to maintain current benefit levels and then next to look for innovative ways to open up the possibility of increasing benefit levels. This may mean a number of different things, but it can not be taken for granted that for some stakeholders the point of this consultation is to do whatever it takes to reduce sponsor costs.

Pensions are not too expensive

The Steelworkers are not opposed to finding effective ways to manage pension funds over the long term but it is our position that pension plans are not too expensive in and of themselves. When we negotiate pensions as a component of our future standard of living, it is because we as workers feel we are owed this standard of living. Furthermore, retirement benefits are not inordinately rich. Benefits for individuals are usually tied in one way or another to the level of compensation that the employer had previously been using to compensate that individual as an employee. For example, benefits for individual retirees are generally a function of that individual's past earnings. In most cases, retirement benefits are geared to the individual's past years of service. In other words, the retirement benefits an individual gets from a company pension are related to how much that employee put into the organization. In these ways, defined benefit pensions, at least in principle, are calculated fairly and reasonably. There is nothing about a worker retiring that suddenly makes a pension too expensive.

Is it really a pension problem?

This is not to say that all employers can always afford their pension contributions. Organizations fare differently. It may be true that a company that is failing can not afford its pension contributions. But when the company is truly failing, it can not afford any of its obligations. There is nothing special in this regard about pension contributions. More to the point, companies do not fail because of their pension obligations. For the most part, companies fail because their core business fails. Companies which have run out of funds before paying their pension

contributions bring with them problems other than pension costs. Obviously, this varies on a case by case basis. But our general principle is that changes to the legislative and regulatory framework that make pensions cheaper to the plan sponsor should only be pursued where it can be shown that it is the defined pension plan framework itself that has made the pension inordinately expensive.

Issues for Discussion

Surpluses

The consultation paper raises a number of questions around surplus and contribution holidays.

The Steelworkers believe that plan surpluses should be used for the exclusive use of plan members. We find it unconvincing that surplus distribution has been a factor in making pensions either non-secure or non-viable.

Many stakeholders will raise the following issues before you. First, changing surplus distribution rules to favour sponsors would increase their incentives to fully fund the plan.

Stakeholders put these issues forward based on the fairly common assertion by plan sponsors and their representatives that an 'asymmetry' exists in which sponsors alone are responsible for funding shortfalls but are prevented from accessing any excess funds. The suggestion is that if sponsors are on the line for the deficit, they should at least get to do whatever they want with the surplus. The Steelworkers do not believe an asymmetry exists and see no benefit in reconsidering the current practices around surplus distribution.

Unionized workers know from experience that employers cost their required pension funding against compensation in general. Funds that go into our pensions are funds that do not go towards our wages or benefits. There is a fairly direct trade-off in practice. For this reason, unionized

workers refer to pensions as deferred wages. As a result, workers have long held that they have a claim to the funds that go into the pension, regardless of whether the plan at any time has a funding surplus or deficit. Pension funds are our compensation funds.

This has been a particularly big issue since the Supreme Court ruling in the Monsanto case, which held that when a defined benefit pension plan is even partially wound-up, a portion of the actuarial surplus must be distributed to plan members. In general, the courts have ruled that once funds are put into the pension, regardless of the funding situation, they in some sense belong to the plan. Accordingly, the courts have agreed that the surplus does not belong in principle solely to the sponsor, and that plan members have at least some claim to the surplus. The Steelworkers understand the Supreme Court decision to be clear and see no need to outmaneuver the basic assumption of the court by changing the policy framework now in order to have a different standard.

We do not believe that the current surplus distribution rules act as a 'disincentive' to adequate funding. To do so would be to second-guess the court. Also, the amount of future retirement benefit owed to current unionized employees is determined as a result of collective bargaining. Once the agreement is ratified, the union's position is that the burden is on the employer to fund this future benefit. For us to engage in a debate now of what we as a union can do in order to give the employer a further incentive to follow-through on their contractual obligations is to second-guess our own bargaining.

Even if we were to engage in such second-guessing, we do not understand our rightful claim to the surplus in certain situations to be in any way a disincentive for the sponsor. One has to first side with sponsor (and against the unions, workers, and the court) on the question of asymmetry in order for the question of incentives to be even relevant.

Lastly, on the question of surplus distribution, we contest whether changing the distribution rules would positively affect funding levels in practice. It is unclear to the union that surplus distribution rules actually have been, or will be, the cause of pension plans failing. It is clear that

reversing the Monsanto decision would make a bottom-line difference in favour of sponsors on partial wind-ups, and therefore it is clear why sponsors would push for this. But the notion that the current rules have actually changed funding decisions, especially when the majority of sponsors are already meeting only the minimum special payments and current service levels, seems rather hypothetical. It is not clear that changing distribution rules would have a concrete effect on either benefit security or plan viability.

The Steelworkers are not in favour of any changes that aim to increase the sponsors' claim on the surplus.

Funding Requirements

As stated at the outset, our understanding of strengthening the pension framework is to ensure security and sustainability. On one hand, our union gains nothing from overly rigid regulations, so we are willing to consider options that would give the sponsors more flexibility. On the other hand, most of the current stakeholder proposals involve the sponsor being able to put down less cash today. This increases the risk for plan members. This risk factor is the main barrier between plan members and acceptance of more flexible funding requirements. Employer groups try to persuade plan members to see it from the employer's position - that is, to believe that lower costs are good for business, which in the end are somehow good for everyone. But plan members are necessarily going to consider their own interests as workers and as future retirees. If the objective is to maintain the same future pension benefit payouts, it is hard to see how smaller payments in the short term by the sponsor make the overall funding target more achievable. Can the pension framework be strengthened simply by appeasing the employer's desire to cut sponsor costs? No.

As stated earlier the union is willing to provide plans sponsors with more flexibility under certain circumstances. We are not interested in providing funding relief for profitable corporations. The current letter of credit schemes that have been adopted under several jurisdictions do just that. The use of letters of credit to reduce funding obligations only benefits those corporations that have the credit worthiness to obtain such credit. They provide little benefit to those corporations

who cannot obtain credit.

The Steelworkers could support extending funding obligations to plan sponsors who find themselves in financial difficulties or exiting from CCAA protection, provided that such extensions could only occur if a majority of plan members or the trade union representing plan members consented to such an extension. In our view such a proposal would provide funding relief were it is most needed.

In our view the best way to pursue flexibility for the sponsor in a way that strengthens the pension framework is to simultaneously counterbalance this change by implementing a Pension Benefit Guarantee Fund similar in design to the plan that currently exists in Ontario. In our view the implementation of such a plan would absorb pension risk from plan members. With the safety that such a scenario would bring, plan members would be much more open to various options that relax funding requirements and provide sponsors with flexibility. A guarantee fund would help eliminate the risk factor for plan members.

The following are some specific suggestions for relating to the design of a pension benefit guarantee fund:

- that maximum individual payouts be as high as $2750 per month
- that benefits be indexed to inflation
- the guarantee fund would be funded through a combination of sponsor premiums that include an additional risk-based premium for plans with unfunded liabilities (for example, an additional premium for plans with a funded ratio under 100%, even more if under 80%)

Grow-in Rights

In our view grow-in rights should be funded on a solvency basis and provided to plan members on plan termination.

Many of our members participate in pension plans that provide unreduced early retirement and bridge benefits. The current practice of not funding grow-in rights does not acknowledge that, during a working lifetime, an employee/plan member accrues an entitlement to early retirement and other ancillary benefits as well as to the normal retirement benefit. When that accrual is interrupted as a result of circumstances beyond the employee's control, that accrual should be recognized based on the employee's seniority and age and included in the termination benefit.

In Nova Scotia, a total or partial plan wind-up triggers benefits for terminated employees that are not available at termination in the absence of a plan wind-up. These benefits are known as "grow-in" benefits and are made available under the "rule of 55". Under the rule of 55, terminating employees whose age and service total 55 or more are entitled to receive the portion of any early retirement benefits that they had earned prior to termination at the date that they would have received them had they continued to work for the employer. However, current legislation only provides grow-in rights if the plan has sufficient funding to pay for them which in general terms means that the plan must be in a surplus position upon termination.

For example, consider a 48-year-old employee with 20 years of service in a plant with 30-year retirement who is terminated in a partial wind-up. In this case, the employee would have been eligible to retire after 30 years of service, at age 58. Under the rule of 55, the employee would be eligible to receive the pension earned as of the date of termination, beginning at the earliest date that he or she would have been eligible to retire had employment not been terminated, in this case age 58. This employee would also be eligible to receive the proportion of any early retirement bridging benefit earned up to the date of termination. Without the grow-in rule and the

rule of 55, the employee would be eligible only for the basic pension benefit beginning at age 65.

Although the description of the benefit can sound quite technical, its significance for individual plan members can be substantial. In the hypothetical case cited above, for example, a normal retirement benefit of $40 per month per year of service and a bridging benefit of $20 per month per year of service would be worth less than half as much without the rule of 55 benefits as it would be with the rule of 55.

We would therefore strongly encourage that the NSPBA be amended to require funding of grow-in benefits.

Minimum Standards

Given that a review of pension legislation has not occurred since 1988 we would also like to discuss some improvements to the current minimum standards.

Vesting of Benefits

In 1988, the “45 & 10” rule of pension vesting was replaced and the Nova Scotia Pension Benefits Act was amended to require pensions to vest as an employee entitlement after only twenty-four months of plan membership. However this change only applied to service accrued after January 1, 1988. This has created pre and post 1987 vesting requirements under the Act. There is a compelling logic to amend the Pension Benefits Act to require immediate vesting upon an employee’s commencement of membership in a pension plan retroactive to the date the member entered the plan. This would eliminate the complicated issue of pre and post 1987 vesting and would also recognize the reality that labour is even more mobile than it was 20 years ago. There is arguably little justification left for requiring employees to participate in a plan for two years before they are guaranteed a pension from their plan.

Pre-retirement Death Benefit

Under current legislation, if a member dies before retirement and after completing 2 years of continuous service, the members surviving spouse or, if none, the member's beneficiary, must be paid at least the commuted value of any pension that has accrued after 1987. The members spouse or beneficiary receives nothing for any pension that has accrued prior to that date. The loss of the accrued pension can have a significant effect on the value of the death benefit payable and must be corrected.

In order to keep this proposal in line with the vesting proposal above we propose that if a member dies before the commencement of his or her pension, the commuted value of all pre and post 1987 pension benefits shall be payable to the members spouse, partner or beneficiary.

Employee representation in pension plan governance

Current legislation provides for the establishment of an advisory committee where a majority of plan members vote to do so. If the majority of the members of the pension plan request the employer in writing to establish an advisory committee, the employer shall establish an advisory committee consisting of at least one representative for each class of employee that is represented in the pension plan.

This is stark contrast to legislation in Quebec, which mandates plan member participation in plan administration. Under Quebec legislation, the pension committee must consist of at least three members, one member designated by active members, one member designated by non-active members and the legal separation in the identity of a plan sponsor and administrator. Clearly these three groups should be included in any amendments to the Act.

We also envision two possible models for employee participation on the administration board in

the NSPBA. The first option, as you discussed in your discussion paper, is the multi employer pension plan (MEPP) model. The MEPP model requires a legal separation between the employer and the administrator in the form of a board of trustees, and for at least half the members of the board to be representatives of plan members.

The second model is to revise Section 14(ii) (b) of the NSPBA to make it a permissive term. This would require the plan administrator to be "a pension committee composed of representatives of members of the pension plan, if a majority of the plan members desired the establishment of such a committee with at least one-half of the being representatives of members of the plan."

The difference between the two models is to leave to negotiation the extent of member participation on the governance structure. The MEPP model being mandatory; the committee model being permissive.

Conclusion

The Steelworkers are thankful to be invited to participate in this open call for consultation. Protecting pensions and improving pension legislation is a very high priority for our union. The positions outlined in this submission are in keeping with the Steelworker goal of protecting the security of defined benefit pensions. They are also in keeping with our understanding of what viability should mean when it comes to everyone's interest in defined benefit pension plans.