

Blakes Bulletin

Pension & Employee Benefits

Alberta/British Columbia Joint Expert Panel on Pension Standards Report

OVERVIEW

The governments of Alberta and British Columbia released the final report of the Alberta/British Columbia Joint Expert Panel on Pension Standards, *Getting Our Acts Together: Pension Reform in Alberta and British Columbia* (the Report) on Friday, November 28, 2008.

Given the fact the Report is 241 pages with 125 recommendations, we have decided, similar to our November 2008 Blakes Bulletin on Pension & Employee Benefits: *Ontario Expert Commission on Pensions Report*, to immediately release a list of the highlights of the Report together with excerpts from the recommendations that relate to the provisions we believe to be of most relevance to our readers. The final report of the Joint Expert Panel on Pension Standards is available on the Alberta Finance and Enterprise at <http://www.finance.alberta.ca> and British Columbia Finance at <http://www.fin.gov.bc.ca>.

We have divided the excerpts from the recommendations into six sections to facilitate readers locating the portions that may be most relevant to their circumstances. These sections include an overview of (i) objectives and regulatory framework that apply to pension legislation in the two provinces, (ii) governance and investment issues, (iii) funding and benefit security issues for both single employer pension plans (SEPPs) and related rules for what the Panel is calling Specified Contribution Target Benefit (SCTB) plans, (iv) specific pension standards, (v) related legal and other frameworks, and (vi) what the Panel is referring to as the ABC Plan, a recommendation designed to establish an occupational pension plan available to all Alberta and British Columbia workers.

Beyond the detailed recommendations, the Report emphasizes the need for not only expanded pension coverage in the two provinces but also promoting confidence in the pension system generally with the adoption of "best practice" standards that have already been developed by Canada's financial regulators for governance and for capital accumulation plans. As well, the Report stresses the need for promotion

and maintenance of harmonization between the two governments' pension legislation through the adoption of identical pension statutes in each province, the establishment of a joint policy advisory council and a joint pension tribunal.

The Report was delivered to the ministers of finance in both British Columbia and Alberta before Friday's broader release. Both provinces are seeking feedback on the Report from interested stakeholders, with a written comment period ending March 2, 2009.

We will be presenting a more detailed discussion of the significant recommendations in the Report at our seminar with Watson Wyatt on December 3 in Calgary and December 4 in Vancouver. (For information, click [here](#).)

For further information on the Report, please contact any member of our [Pension & Employee Benefits Group](#).

HIGHLIGHTS

- The governments of Alberta and British Columbia should work together to fully harmonize pension standards legislation in the two provinces, resulting in each province enacting identical pension standards legislation.
- The governments of Alberta and British Columbia should create joint organizational structures that would foster continued harmonization of pension standards legislation in the two provinces, including a joint pensions tribunal, a joint pensions advisory council, and a joint pension regulator.
- The governments of Alberta and British Columbia should establish a "pension advocate" who is responsible for promoting pension coverage in the two provinces.
- The principles contained in the CAPSA Governance Guidelines should be adopted as a schedule to the legislation in a way that explicitly incorporates the Guidelines into pension law in the two provinces.
- Every pension plan should be required to have a governance policy approved by the governing parties, which should be disclosed to members and made available to the regulator for inspection upon request.

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- Every pension plan that includes either a defined benefit (DB) or "target" benefit provision should be required to have a funding policy as part of its governance policy, which should be disclosed to members and made available to the regulator for inspection upon request.
- Both provinces investment standards should be "uncoupled" from the investment rules in Schedule III of the federal Pension Benefits Standards Regulation, 1985 (Canada) to remove quantitative restrictions on investment and increase reliance on the prudent investor principle.
- The existing "prudent person rule," with respect to investment of pension plan assets, should be expanded to incorporate a requirement for expertise.
- Plan fiduciaries for both defined contribution (DC) and DB plans, who can demonstrate they are compliant with the requirements of a "pension judgment rule," should have a statutory defence against claims in respect of their decisions in the same manner that corporate directors are protected by the business judgment rule.
- Current going-concern funding rules should continue to apply and be determined by the plan actuary and the plan sponsor, based on the plan's funding policy.
- Solvency valuations should be required annually unless, at any valuation, plan solvency was 110% or greater, in which case the next valuation would not be required for three years.
- Solvency valuations should be prepared on a purely wind-up basis, assuming annuity purchases are for persons receiving a pension or such persons are eligible to receive an immediate pension. Discretionary benefits should not be included in the valuation and assets should be valued based on pure market measures (with no smoothing of assets).
- Amortization of any solvency deficiency should continue to be over five years; however, assets to satisfy the deficiency could include letters of credit or assets in a "pension security fund" (PSF) that would be separate from but complementary to the regular pension fund.
- The PSF is voluntary and would receive contributions required to meet solvency obligations over and above the going-concern obligations of the plan.
- The PSF would also hold voluntary sponsor contributions greater than those required to meet solvency obligations, to assist in managing contribution volatility, and could be structured as a trust, insurance contract or other financial funding medium acceptable under the federal Income Tax Act.
- Contribution holidays and surplus withdrawals from the regular pension fund should be permitted, unless explicitly prohibited in the plan terms or upon member and regulator consent.
- Contribution holidays and surplus withdrawals should be restricted to ensure they do not reduce surplus assets to less than 5% of the value of the liabilities as of the most recent review date, and both contribution holidays and surplus withdrawals should be required to be spread over five years (20% of the excess per year).
- The financial position of the plan should be required to be updated (based on changes in interest rates and actual investment returns) before surplus can be withdrawn or a contribution holiday can commence. An annual financial update of the financial position of the plan, the amount of the 5% buffer and the amount of the surplus available should be required in subsequent years (i.e., years two to five) before the surplus withdrawal or contribution holiday can continue.
- Where the PSF has been established, a contribution holiday should be permitted in the regular pension fund to the extent that funds are in excess of the going-concern requirements and as long as the sum of the regular pension fund plus the PSF (after the contribution holiday) exceeds the funds needed under the solvency valuation based on a 105% threshold.
- Letters of credit should continue to be permitted for use in securing solvency deficiency obligations.
- Plans with "legacy" surplus issues should be permitted to "ring fence" such issues by allowing the older plans to be frozen and new plans to be established with clear contractual provisions relating to surplus issues to "wrap around" the frozen plan under specific conditions.
- On a plan merger or division, a plan is permitted but not required to transfer a proportionate share of surplus, and all surplus transferred to the new plan will be subject to the terms of the new plan.

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- Where a plan has been converted from DB to DC leaving a legacy DB provision in place within the plan, surplus arising with respect to the DB provision should be available for employer contribution holidays in the DC portion of the plan as long as the DB and DC segments are part of the same trust (to the extent that the plan assets are subject to a trust).
- Plan expenses should be payable from the plan fund unless the terms of the plan specifically require otherwise.
- A new set of funding, disclosure and benefit rules for single and multi-employer plans with similar characteristics called "specified contribution target benefit" (SCTB) plans will come with a single funding test for the purpose of setting minimum funding standards under a "going-concern plus" test.
- The actuary to a SCTB would have to demonstrate that the plan has appropriate Provision for Adverse Deviation (PfAD) variables, which should include liabilities between active and deferred/retired members, degree of mismatch between assets and liabilities, and the variability of hours worked, i.e., the greater the volatility of the above variables, the greater the PfAD.
- If going-concern liabilities plus any necessary PfAD are greater than the assets, deficiencies should be required to be eliminated by increasing contributions and/or reducing benefits in order to restore the plan to a targeted funded ratio with the plan having to demonstrate that contributions would be sufficient to amortize unfunded liabilities over 15 years or the "expected average remaining service life," whichever is less.
- No benefit improvement should be permitted for an SCTB plan unless there is at least a 100% going-concern plus funded ratio, and no benefit improvement should be allowed that would reduce the plan's funded status below the fund's target ratio.
- As with other governance recommendations, a funding policy should be mandatory for all SCTB plans and must include a policy on benefit increases, as well as require that the actuary opine that there is nothing in the funding policy that is inconsistent with sound actuarial practice for the particular plan.
- The maximum termination benefit an individual can receive from an SCTB plan is 100% of the going-

concern liability. If the funded ratio of the SCTB plan is less than 100%, terminating members who elect to transfer their funds out of the plan will receive a pro-rated amount based on the funded ratio. There is no subsequent additional payment to increase the amount paid to the terminating member to the target benefit.

- It should be optional whether a plan permits unlocking but if it does, individuals who are at least age 50 should be permitted to unlock either 25% or 50% of their entitlements, on a one-time basis, at or after termination of employment. If the plan is silent on unlocking, then 50% unlocking at age 50 should be the default and there should be no change to the existing unlocking rules (subject to harmonization) with respect to shortened life expectancy, non-residency in Canada and small amounts.
- The British Columbia and Alberta governments should encourage the federal government to extend the "super priority" secured creditor status to all due but unpaid contributions, including solvency deficiencies or unfunded liability special payments, but not to extend such status to amounts that are unamortized but not yet due.
- The British Columbia and Alberta governments should encourage the federal government to raise the maximum contribution/benefit limits and to raise the maximum funding limits to allow surpluses of up to 25%.
- There should not be a pension guarantee fund in Alberta and British Columbia.
- The governments of British Columbia and Alberta should both establish a steering committee made up of experts in pension plan administration, governance and investment to examine the feasibility of establishing a multi-employer pension plan available to all employers and employees working in our provinces. This plan, referred to as the ABC Plan, should be based on a simple DC formula with matching employer and employee contribution rates and should be a voluntary system with auto-enrolment with opt-out provisions for both employers and employees, including an opt-in provision for the self-employed. Governance and administration of the ABC Plan should be at arm's length from government.

The detailed excerpts from the recommendations now follow.

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I. OBJECTIVES AND REGULATORY FRAMEWORK

OBJECTIVES OF THE LEGISLATION

Recommendation 6.1-A The governments should commence a comprehensive re-write of the EPPA and the PBSA based on the recommendations contained in this report.

Recommendation 6.1-D The legislation should have the following primary objectives:

- facilitating coverage by reducing barriers causing sponsors to be unwilling or unable to establish or maintain occupational pension plans
- setting streamlined minimum pension standards with effective enforcement powers, while providing maximum flexibility, simplicity and clarity to facilitate the establishment and maintenance of plans
- avoiding over-regulation that could deter employers from participating in the occupational pension system
- ensuring that pension promises made in this new context are kept

Recommendation 6.1-F Pension standards legislation should address all currently foreseeable matters relating to pensions, including those that have been considered by the courts to date, in order to incorporate those matters into a comprehensive legislative framework to the extent possible.

Recommendation 6.1-G Where professional standards are to become legislative requirements, they should be specifically identified, and changes should be adopted only if reviewed and agreed to by the governments.

Principles-based vs. rules-based legislation

Recommendation 6.2-A Pension standards legislation in Alberta and British Columbia should be reconstructed to adopt an approach employing principles wherever possible, supported by detailed rules where necessary. Elements of this approach include:

- principles setting certain criteria of general application, regardless of plan type;
- rules-based standards in some specific areas; and
- different rules applicable to different types of plans, as appropriate. (See also Section 6.3 "Alternative Plan Designs" below.)

Recommendation 6.2-B Where principles are appropriate, they should be set out in the pension standards statute, supported by more detailed rules that may be subject to more frequent change in the regulations, to ensure that sponsors can manage plans in a manner that provides some confidence as to their obligations.

Recommendation 6.2-C Regulatory policies and guidelines should be developed to provide guidance to plan sponsors, administrators and members on compliance with principles-based standards.

Recommendation 6.2-D The regulator should have the discretion and resources necessary to properly fulfill its role in the context of a principles-based system. (See also Section 6.4 "Role of the regulator" below.)

Recommendation 6.2-E In light of the recommended increase in the discretion of the regulator in a more principles-based system, an adjudicative body should be established to hear appeals from the exercise of that discretion, acting as a "check and balance" within the regulatory system. (See also Section 6.4 "Role of the regulator" and Section 6.5 "Harmonization" below.)

Recommendation 6.2-F Future refinement of the principles in the legislation and the regulatory interpretation thereof should be developed in consultation with an appropriate pension policy advisory body. (See also Section 6.4 "Role of the regulator" and Section 6.5 "Harmonization" below.)

ALTERNATIVE PLAN DESIGNS

Recommendation 6.3-A The legislation should contain principles of general application to all pension plans, including, without limitation, principles dealing with eligibility to participate, vesting of entitlements, locking-in of benefits, portability of benefits, segregation of assets, the role and identity of the governing fiduciary and how the "pension deal" is to be defined.

Recommendation 6.3-B Different rules should be developed that are appropriate to different existing and future plan types, and such rules should be housed in regulation and/or regulatory policy.

Recommendation 6.3-C The next generation of pension standards legislation in Alberta and British Columbia should be designed to permit flexibility in the development of new plan design types, subject to adherence to the principles of general application.

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ROLE OF THE REGULATOR

Recommendation 6.4-A The legislation should be clear that the role of the regulator is to administer and enforce compliance with the legislation, and not to actively promote pension coverage.

Recommendation 6.4-B The regulator's role should focus on risk-based monitoring to encourage and enforce compliance with principles-based standards and prescribed rules.

Recommendation 6.4-C The regulator should be provided with sufficient resources to transition personnel and culture to this new model with appropriate training and education.

Recommendation 6.4-E The regulator should have discretion under the legislation to consider applications for approval of new plan designs and governance structures applying the principles of general application set out in the legislation and to impose such conditions on registration as may be appropriate in the circumstances and consistent with the principles. (See also Section 6.4.1 "Regulator's tools and checks and balances in the system" below.)

Recommendation 6.4-F The regulator should develop administrative policies and guidelines on a collaborative basis with input from the broader pension community, in order to provide guidance on the interpretation of the principles-based standards contained in the legislation.

Recommendation 6.4-G The governments should establish the position of a "pension advocate," whose role would be to promote the pension system and the expansion of pension coverage in Alberta and British Columbia. (See also Section 6.5.2 "Joint Pension Advisory Council" below.)

REGULATOR'S TOOLS AND CHECKS AND BALANCES IN THE SYSTEM

Recommendation 6.4.1-A The regulator should have the power to impose administrative penalties, subject to the following conditions:

- Penalties should only be imposed with proper advance notification in writing that the penalty is intended to be applied and providing a reasonable opportunity for the matter at issue to be "cured" before the penalty is imposed.

- The penalties could be imposed for failure to:
 - file annual information returns on time;
 - file valuation reports on time;
 - file annual financial statements on time;
 - respond to superintendent requests for information on time;
 - disclose information to members on time; or
 - make contributions on time.
 - Proceeds of fines should be used to finance the regulatory system and should not be directed to the governments' general revenues.
 - The authority to impose penalties should be discretionary depending on the circumstances for significant issues of non-compliance or to encourage appropriate plan management/governance, and not as punishment other than in egregious situations.
 - Penalties should be imposed on the party responsible for the matter or action at issue, typically the plan administrator, and should not be charged to or be payable from the plan.
 - The imposition of the penalty should be subject to appeal. (See also Section 6.5.1 "Joint Pension Tribunal" below.)
- Recommendation 6.4.1-B** The regulators should be provided with discretion to approve new plan designs and associated governance structures in the following manner:
- The process for approval of new plan designs should be set out in the legislation.
 - The legislation should provide the superintendents with the discretion to make guidelines of general application to plans with certain common design features.
 - Where the regulator intends to impose conditions of general application for a new type of plan in connection with specific features that are not contemplated in the legislation, consultation with a policy advisory body (to be established by the governments) should be required. In publishing such guidelines, the regulator should identify the particular elements that make the new model different and justify the creation of the guidelines.

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(See also Section 6.5.2 "Joint Pension Advisory Council" below.)

- Regulators' decisions on plan approvals should be subject to appeal. (See also Section 6.5.1 "Joint Pension Tribunal" below.)
- The legislation should prescribe considerations or conditions that the regulator must take into account in exercising the decision-making discretion.
- In order to encourage and maintain consistency between the two provinces, consultation between the regulators in Alberta and British Columbia should be mandated as a matter of policy of the two governments prior to the issuance of any approval or rejection of a new plan design, or the publication of a guideline of general application. (See also Section 6.5 "Harmonization" and Section 6.5.3 "Joint pension regulator" below.)

Recommendation 6.4.1-C The governments should each establish an independent expert administrative tribunal, preferably on a joint basis, to hear appeals from superintendents' decisions. Such a tribunal should be authorized to hear appeals from any decision of the regulator by a party to the issue at hand. (See also Section 6.5.1 "Joint Pension Tribunal" below.)

Recommendation 6.4.1-D The governments should establish a joint policy advisory council to provide broad input and insight to the ministers responsible for pension standards in the two provinces and to the regulators, in respect of matters of pension policy and compliance on an ongoing basis. (See also Section 6.5.2 "Joint Pension Advisory Council" below.)

HARMONIZATION

Recommendation 6.5-A The governments work together to fully harmonize pension standards legislation in Alberta and British Columbia, resulting in identical statutes with the same name in the two provinces.

Recommendation 6.5-C The rule of "final location" should be confirmed in Alberta's and British Columbia's pension standards legislation to ensure that the laws of the jurisdiction in which a plan member worked last apply to that person's benefits, regardless of where the pension credits were actually earned.

Recommendation 6.5-D The governments should work together to create joint organizational structures that would foster continued harmonization of pension

standards legislation in the two provinces, including a Joint Pensions Tribunal, a Joint Pensions Advisory Council and a joint pension regulator. (See also Sections 6.5.1 through 6.5.3 below.)

JOINT PENSION TRIBUNAL

Recommendation 6.5.1-A The governments should work together to establish a Joint Pension Tribunal having the following characteristics:

- The JPT should be a statutory body constituted under the statutes in each province, with quasi-judicial status.
- The JPT should be established on the "common member" model.
- The harmonized legislation should include a strong privative clause, such as that contained in subsection 242.3(2) of the British Columbia Financial Institutions Act, to ensure the maximum possible deference by the courts in favour of decisions issued by the JPT.
- The JPT should be dedicated to pension matters only, to preserve its status as an expert tribunal in the eyes of the courts, thereby also enhancing the deference paid to its decisions.
- The purpose of the JPT should be to hear appeals from administrators and other "applicants" (being any party who has submitted a plan for registration, or any other person subject to the directive powers of the regulator) in respect of decisions of the regulator.
- The JPT should be independent and at arm's length from the governments.
- The JPT should be bound by and able to establish precedents.
- The JPT should have balanced representation from both provinces.
- Members of the JPT should be appointed by the Lieutenant-Governors-in-Council in both provinces.
- The membership of the JPT should consist of a chair, vice-chair and other members, all of whom are recognized pension experts.
- The chair and vice-chair of the JPT could ultimately be full-time positions once appeal volumes are sufficient to justify it.
- There should be multiple members appointed, sufficient to respond to cases in a timely manner.

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JOINT PENSION ADVISORY COUNCIL

Recommendation 6.5.2-A The governments should work together to establish a Joint Policy Advisory Council having the following characteristics:

- The JPAC should be a statutory body created under the pension standards statutes in each of the provinces, and its members should be remunerated according to government guidelines.
- The JPAC should be established on the "common member" model.
- The stated purposes of the JPAC should be to:
 - provide policy advice to the ministers and the superintendent(s);
 - recommend changes to the legislation in both provinces as needed and provide input and advice on proposed amendments;
 - provide advice to the superintendent(s) on the administration of the legislation and the development of regulatory policies and guidelines;
 - promote continued harmonization between Alberta and British Columbia; and
 - encourage national harmonization.
- The JPAC should be appointed jointly by and report to the two ministers on a regular basis in respect of its activities.
- There should be balanced representation from both provinces in the membership of the JPAC.
- The JPAC should be of a workable size that is not too big, for example with a maximum of nine members.
- Membership on the JPAC should include representation from among pension plan sponsors, pension plan members and pensioners, professional service providers and government policy staff, with the superintendent(s) sitting on the JPAC in an "ex officio" capacity.

• The position of chair of the JPAC should be a permanent position, designated as the "Pension Advocate", and be responsible for and accountable to the ministers with respect to:

- chairing the Council;
- promoting awareness of pensions, pension policy and retirement income planning among employers and employees, and promoting the expansion of pension coverage; and
- promoting financial education with respect to pensions and retirement savings.

• Membership on the JPAC, other than the chair, should be for fixed staggered terms, resulting in regular turnover in membership.

JOINT PENSION REGULATOR

Recommendation 6.5.3-A The governments work towards the establishment of a joint pension regulator to administer and enforce, on a consistent basis in both provinces, the recommended harmonized pension standards legislation.

II. GOVERNANCE AND INVESTMENT

GOVERNANCE STANDARDS

Recommendation 7.1-A The principles contained in CAPSA's governance guidelines should be adopted as a schedule to the legislation, in a way that explicitly incorporates them into pension law and makes them straightforward to update, as necessary. (See also Recommendation 6.1-G regarding adoption of professional standards.)

Recommendation 7.1-B Every plan should be required to have a governance policy. Plan governance policies should be required to be:

- approved by the governing parties;
- updated regularly;
- brought to the attention of members and other beneficiaries;
- available upon request to all members and other beneficiaries; and
- available to the regulator upon request, but not required to be regularly filed.

Required elements of a plan governance policy should be specified, possibly in regulation – similar to the rules relating to the contents of a Statement of Investment Policies and Procedures (SIPP). At a minimum, plan governance policies should include:

- a profile of the pension plan: a summary of the plan's key features, its purpose, who makes contributions and how they are determined, how benefits are defined and determined and how the fund is established, held, managed and invested;
- a description of the key elements of the governance structure: the composition of any board, and the basis on which decisions are made and implemented;
- a summary of how business is to be conducted: timing, location and frequency of meetings, how a quorum is obtained, how meetings are to be recorded and how the voting system is to operate;
- a detailed description of the roles and responsibilities of each party included in the governance structure;
- a description of when and how the administrator may employ agents and advisors in carrying out its duties,

including standards for the appointment, reporting requirements and evaluation of such agents or advisors;

- a listing of stakeholders and a description of their interests in the plan;
- the standards of performance expected of the administrator (including those expected of trustees, both individually and collectively), including:
 - a code of conduct that addresses expectations for meetings, relationships between trustees, with agents/advisors and with members
 - a policy regarding conflicts of interest
 - an assessment of educational requirements and training needs for those who have responsibility for aspects of plan administration
 - planning and performance measures
 - the use of agents and advisors
 - communication to stakeholders
- a funding policy (see also Recommendation 7.1-C below);
- a SIPP (already required in current legislation); and
- a remuneration and expense policy for trustees, if applicable.

Recommendation 7.1-C Every pension plan that includes either a DB or "target" benefit provision should be required to have a funding policy. The funding policy should be part of governance policy and should be made available to the regulator for inspection upon request. However, it should not be required to be filed. Necessary elements of a plan funding policy should be specified, possibly in regulation – similar to the contents of a SIPP. At a minimum, plan funding policies should include:

- an explanation of the purpose of the policy;
- a summary of the risks to which the plan's funded status is exposed;
- a description of the policies adopted to protect the plan's funded position against the risks identified (e.g. asset valuation methodology, how economic assumptions are developed, funding margins, funding thresholds for benefit increases and decreases); and

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- an explanation of how the funding policy was developed (the rationale for the policy selected to protect the plan's funded position against the risks identified).

INVESTMENT RULES

Recommendation 7.2-A Alberta and British Columbia investment standards should be "uncoupled" from the federal Schedule III, to remove quantitative restrictions on investment and increase reliance on the prudent investor principle.

Recommendation 7.2-B Specific rules in Schedule III that protect against conflicts of interest (related party rules) should be integrated into provincial legislation.

Recommendation 7.2-C The existing "prudent person rule" with respect to investment of pension plan assets should be expanded to incorporate a requirement for expertise. Plan assets should be invested in a manner similar to the way in which a prudent expert would invest them. If the required expertise is not possessed by the governing fiduciary, the plan should be required to seek and avail itself of an appropriate level of expertise, but must still have sufficient knowledge to understand and question the advice.

FIDUCIARY PROTECTION

Recommendation 7.3-A Elements of the CAP Guidelines that do not relate to investment choice should be legislated to apply equally to all plans, including those that do not offer member investment choice. (See Recommendation 7.1-A above)

Recommendation 7.3-B The legislation should explicitly state that "auto-enrolment" and "auto-escalation" are permitted and are not actionable in and of themselves.

Recommendation 7.3-C The provision of one investment vehicle only should not, in itself, be actionable unless the selection has not been made and monitored with due diligence.

Recommendation 7.3-D Plan fiduciaries who can demonstrate that they are compliant with the requirements of a "pension judgment rule" in the legislation should have a statutory defence against claims in respect of their decisions in the same manner that corporate directors are protected by the business judgment rule.

III. FUNDING AND BENEFIT SECURITY

DEFINED BENEFIT FUNDING RULES

Recommendation 8.1.1-A Pension standards should continue to require both solvency and going-concern valuations, with reasonable requirements that protect benefit security while not being overly onerous for sponsors, as further described below:

Going-concern funding requirements

Recommendation 8.1.1-B Current going-concern funding rules should continue to apply and be determined by the plan actuary and the plan sponsor, based on the plan's funding policy (see also Section 7.1 "Governance standards" above), actuarial standards of practice and regulatory requirements.

Solvency funding requirements

Recommendation 8.1.1-C Solvency funding rules should be developed on the following bases:

- Asset valuations should be based on pure market measures (with no smoothing of assets).
- Liability valuations should be prepared on a pure wind-up basis, assuming annuity purchases for persons receiving or eligible for immediate pensions and termination (commuted) values otherwise. Benefits provided at the discretion of the administrator/trustee/plan sponsor should not be included in the valuation.
- Assumptions should be based on the actuarial standards for calculating commuted values that would be adopted in the legislation. (See also Recommendation 6.1-G above.) No additional margins or provisions for adverse deviation (PfADs) should be required, other than those already implicit in the commuted value.
- Amortization of any solvency deficiency should continue to be over five years; however, assets to satisfy the deficiency could include letters of credit or assets in a PSF. (See Recommendations 8.1.2-A and 8.1.2-C below.)
- Solvency valuations should be required annually unless, at any valuation, plan solvency was 110 percent or greater, in which case the next valuation would not be required for three years.

OWNERSHIP AND USE OF SURPLUS

Pension Security Funds

Recommendation 8.1.2-A Pension standards legislation should permit the establishment of a "pension security fund" (PSF) that would be separate from but complementary to the regular pension fund, on the following bases:

- Contributions required to meet going-concern funding obligations should be forwarded to the regular pension fund as under current practice.
- Contributions required to meet solvency obligations over and above the going-concern obligations could be forwarded to the PSF.
 - The PSF should be:
 - tax sheltered, held separate from the sponsor's assets and protected from creditors;
 - accessible to the plan sponsor with regulator consent:
 - as long as the sum of the regular pension fund plus the PSF (after access by the sponsor) exceeds the funds required to meet solvency requirements, with a five percent cushion, and the withdrawal is spread over a five-year period (20 percent of the excess per year)
 - based on a current valuation within one year of the most recent valuation date
 - but only if an actuarial certification that there has not been a material change since the valuation date is provided
 - returned to the plan sponsor on plan windup, to the extent not needed to meet benefit obligations and windup expenses.
 - The PSF could also hold voluntary sponsor contributions greater than those required to meet solvency obligations, to assist in managing contribution volatility.
 - The PSF could be structured as a trust, insurance contract or other financial funding medium acceptable under the federal Income Tax Act. (See Section 10.1 "Income tax rules" below.)
 - The governments should consult with the CIA regarding detailed rules on PSFs (including certification requirements and frequency of valuations).

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Contribution holidays/surplus withdrawals – regular fund

Recommendation 8.1.2-B Contribution holidays in relation to, and surplus withdrawals from the regular pension fund would be permitted, on the following bases:

- Contribution holidays should be permitted unless explicitly prohibited in the plan terms.
- Surplus withdrawal from the regular fund should continue to be permitted subject to regulator consent and only if the plan permits it or the members consent.
- Contribution holidays and surplus withdrawals should be restricted to ensure that they do not reduce surplus assets to less than five percent of the value of the liabilities as of the most recent review date.
- The financial position of the plan should be required to be updated (based on changes in interest rates and actual investment returns) before the withdrawal can be made or the contribution holiday can commence.
- Both contribution holidays and surplus withdrawals should be required to be spread over five years (20 percent of the excess per year).
- For the holiday or the withdrawal to continue after the first year, the financial position of the plan, the calculation of the five percent buffer and the amount of the surplus available should be required to be updated annually in a similar manner.
- Where a PSF had been established, a contribution holiday should be permitted in the regular pension fund:
 - to the extent that funds are in excess of going-concern requirements; and
 - as long as the sum of the regular pension fund plus the PSF (after the contribution holiday) exceeds the funds needed under the solvency valuation based on a 105 percent threshold.

See Section 10.1 for recommendations relating to income tax limits on surplus assets.

Letters of credit

Recommendation 8.1.2-C Letters of credit should continue to be permitted for use in securing solvency deficiency obligations.

Legacy surplus issues

Recommendation 8.1.2-D Plans with “legacy” surplus issues should be permitted to “ring-fence” such issues

by allowing the older plans to be frozen and new plans to be established with clear contractual provisions relating to surplus issues to “wrap around” the frozen plan, on the following bases:

- The terms and conditions of the new plan with respect to surplus use and withdrawal should be subject to contract law.
- The existing plans, whose surplus use and withdrawal rules were governed by trust law, should be permitted to be closed to new entrants and frozen with respect to accruals of further service and recognition of salary increases.
- Recognition of vesting and other entitlements in the old plan should be required for the purpose of establishing benefit entitlements in the new plan, and vice versa.
- Benefits in the new plan should include recognition of salary increases with respect to service accrued in the frozen plan.
- There should be no requirement to wind up the “legacy” plan, but rather it would continue and form part of the members’ ultimate benefits from the two combined plans, continuing to pay out benefits until all liabilities are discharged.

UTILIZATION OF PLAN ASSETS

General rules

Recommendation 8.1.3-A The governments should adopt the following principles in the legislation for asset utilization:

- Established property rights to surplus that is in a plan at termination should not be tampered with.
- At all times if a pension plan sponsor and members want to define their “deal” regarding surplus ownership and utilization in some other fashion, they should not be precluded from doing so.
- Surplus in an ongoing plan should be available to the plan sponsor for contribution holidays unless the plan explicitly prohibits it.
- Withdrawal of surplus by the plan sponsor should take place only if the plan permits it or the employees agree; the withdrawal should be subject to regulator approval.
- Surplus in new “wrap-around” plans and in

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PSFs should be dealt with as described in the Recommendations under Section 8.1.2 above.

The governments should build upon these principles as the body of common law evolves with subsequent court decisions.

Partial plan terminations

Recommendation 8.1.3-B The following rules should apply with respect to surplus use and distribution on partial plan terminations:

- Vesting of benefits should be automatic for all members affected by a partial termination but vesting should not include a right to surplus assets unless the plan specifically provides for it.
- Partial terminations should continue to be required, subject to the criteria in the current legislation (termination of an identifiable group, etc.).
- Administrators should be required to notify the regulator of a plan termination rather than being required to file a special report; the actuary of a DB plan should also report the event on a subsequent regular valuation.

Plan mergers and divisions

Recommendation 8.1.3-C The following rules should apply to plan mergers and divisions:

- A plan should be permitted, but not required, to transfer a proportion of the surplus equal to the ratio of the liabilities for the transferred members to the total of the plan's liabilities.
- The money transferred into the transferee plan should be allowed to be used according to the terms of the new plan.

Plan expenses

Recommendation 8.1.3-D Plan expenses should be payable from the plan fund unless the plan text specifically provides otherwise. This default rule would supplement the current standard requiring all plan texts to contain a provision indicating how plan expenses will be paid. It would address problems in old plans with unclear or nonexistent wording.

DB/DC contribution holidays

Recommendation 8.1.3-F Where a plan has been converted from DB to DC leaving a legacy DB provision in place within the plan, surplus arising with respect

to the DB provision should be available for employer contribution holidays in the DC portion of the plan as long as the DB and DC segments are part of the same trust (to the extent that the plan assets are subject to a trust).

SPECIFIED CONTRIBUTION TARGET BENEFIT PLANS (SCTB)

Funding rules for SCTBs

Recommendation 8.2.1-A A new category should be created in the pension legislation for funding and disclosure for single and multi-employer plans with similar characteristics, called specified contribution target benefit plans. The essential characteristics of such a plan are:

- Contributions are limited to specified employer and employee contributions ("specified" by the parties to the deal, whether through a collective bargaining agreement or another method).
 - Employer(s) are limited in their liability to providing the specified contributions.
 - There is a formula benefit set out in the plan document but it is subject to reduction if funding is not sufficient and can therefore be considered a target benefit.
- Recommendation 8.2.1-B** There should be a single funding test for the purpose of setting minimum funding standards. It should be a "going-concern plus" test:
- Going-concern liabilities should be estimated using "best estimates" of long-term going-concern assumptions, following generally accepted actuarial practice.

- The actuary should have to demonstrate that the plan has an appropriate PfAD. The variables at issue could include, but not necessarily be limited to:

- distribution of liabilities between active and deferred/retired members,
- degree of mismatch between assets and liabilities, and
- variability of hours worked

The greater the volatility of the above variables, the greater the PfAD needed. The result would be a target

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going-concern funded ratio of 100 percent at minimum, rising with the degree of PfAD.

- The funding rules should either specify the magnitude of the PfAD or incorporate actuarial standards addressing the same issue. As actuarial standards are yet to be developed in this area, the CIA should be asked to develop such standards or at least to advise legislators on appropriate PfAD standards.

Recommendation 8.2.1-C To determine the size of the PfAD and the prescription for remediating problems, the funding rules should require that stress testing be performed as part of the actuarial valuation:

- The standards should require the actuary to perform all appropriate scenario tests which must include both stochastic tests, and specified deterministic scenarios.
- Standards for stochastic testing should have to state what level of statistical confidence would be required.
- Where the plan would be vulnerable to the failure or withdrawal of one or more employers, that scenario should be included in the stress testing. Proportionate and appropriate protection should be factored in when there is an apparent significant chance of wind-up.
- It is important that the actuarial profession be engaged to develop stress testing metrics. Actuarial standards do not currently exist in this area; therefore, the CIA should be asked to create such standards. If the profession declines to create such standards, the legislation should impose them based on advice from actuarial consultants.

Recommendation 8.2.1-D If going-concern liabilities plus any necessary PfAD are greater than assets, deficiencies should be required to be eliminated by increasing contributions and/or reducing benefits so as to restore the plan to the target funded ratio. The remediation should be required to be achieved with regular, consistent and timely treatment:

- The plan should have to demonstrate that contributions would be sufficient to amortize unfunded liabilities over 15 years or the "expected average remaining service life", whichever is less. The other rules relating to unfunded liabilities would continue to apply:
 - Once identified, an unfunded liability should be required to be amortized in that length of time or less and should not be allowed to be

combined with more recently established unfunded liabilities so as to extend the amortization period beyond the original maximum period.

- Gains should be required to be applied to the oldest-established unfunded liability first, with the result that either the payments would be lowered or eliminated, or the same payments would continue but the unfunded liability would be amortized more quickly.
- If funding levels indicated above are not met, the plan's funding status should be required to be adjusted immediately by contribution increases, changes in plan design (e.g. benefit reductions or increased eligibility requirements) or a combination of those. The trustees should have the primary responsibility to exercise even-handedness in making any changes in plan design.

Benefit improvements for SCTBs

Recommendation 8.2.2-A The legislation should also require that a reasonable method be used for costing benefit improvements: benefit improvements should be valued on the same going-concern-plus basis as required for the minimum funding standards.

Recommendation 8.2.2-B No benefit improvement should be permitted unless there is at least a 100 percent going-concern-plus funded ratio and no benefit improvement should be allowed that would reduce the plan's funded status below the fund's target ratio.

Recommendation 8.2.2-C To provide more flexibility in plan design, temporary benefit improvements should be permitted, subject to the general limitation that there must be a going-concern-plus surplus. These improvements must be accompanied by full disclosure to plan members of the temporary nature of the benefit and who is entitled to receive it. Such improvements should be subject to Recommendation 8.2.2-B limiting benefit improvements.

Valuations for SCTBs

Recommendation 8.2.3-A The current standards for frequency of valuations should be retained. The regulator should continue to have discretion to require more rigorous and/or more frequent valuations and/or additional stress testing as part of risk-based monitoring.

Recommendation 8.2.3-B In any SCTB plan where the probability of wind-up is higher, the actuary should be

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required to take into account the wind-up scenario in setting the going-concern-plus assumptions. The more probable the windup scenario the closer the going-concern-plus valuation should be to a wind-up valuation.

Recommendation 8.2.3-C The valuation filed with the regulator should state the target funded ratio and how it was calculated, including making the PfAD explicit.

Recommendation 8.2.3-D The valuation should be required to include an estimate of the amount that would be required to settle all liabilities at that point in time (settlement valuation), and state the settlement ratio.

Transfer values

Recommendation 8.2.5-A An individual's termination benefit should be valued using the same assumptions as were used in the most recent valuation, that is, on a going-concern-plus basis.

Recommendation 8.2.5-B The maximum termination benefit any individual may receive should be 100 percent of the going-concern liability. Even if the current funded ratio is over 100 percent to meet the plan's target funded ratio, the maximum payment should be 100 percent. If the ratio is less than 100 percent, terminating members who elect to remove their funds should receive a pro-rated amount, based on the funded ratio at that time. There should be no later "catch-up" payment to bring their payment to 100 percent of the target benefit.

SCTB governance

Recommendation 8.2.6-A Our recommendations relating to governance standards in Section 7.1, and trustee/fiduciary education in Section 7.1.1, should be adopted to complement these funding rules. We do not endorse any single governance structure as the most suitable.

Recommendation 8.2.6-B As indicated in Recommendation 7.1-C, a funding policy should be a mandatory element of the governance policy for these plans. Some of the special requirements related to funding policies for SCTBs should include:

- There should be a policy on benefit increases.
- The legislation should require that the actuary, in the actuarial report, opine that there is nothing in the

funding policy that is inconsistent with sound actuarial practice for the particular plan.

Recommendation 8.2.6-C The governing fiduciary should be required to certify that the plan has been managed in accordance with its governance policy, funding policy and investment policy.

Recommendation 8.2.6-D There should be a requirement for an annual assessment by the governing fiduciary of the plan's administration, its compliance with legislated minimum standards, governance, funding and investment policies, and the performance of the trustees, administrative staff and significant external professionals. The assessment should be in writing and available to the regulator upon request, but should not be required to be filed.

Recommendation 8.2.6-E Governing fiduciaries should be required to obtain the education and training required in order to properly meet their responsibilities. (See also Recommendation 7.1.1-B.)

Recommendation 8.2.6-F Governing fiduciaries should be required to ensure that those with administrative responsibilities with respect to the plan are appropriately trained.

IV. SPECIFIC PENSION STANDARDS

LOCKING IN

Recommendation 9.1-A Unlocking of funds subject to pension standards legislation in Alberta and British Columbia should only be permitted on the following bases:

- Pension funds should remain locked in so long as the individual is still an active member of the plan.
- SCTBs should retain the ability to set rules regarding when an individual is or is not a terminated member.
- It should be optional whether a plan permits unlocking.
- If a plan permits unlocking, individuals who are at least age 50 should be permitted to unlock either 25 percent or 50 percent of their entitlements, on a one-time basis, at or after termination of employment. The unlocked amount could be transferred to a non-locked in RRSP, while the locked in portion could be transferred to a LIRA or locked-in RRSP.
- If the plan is silent on unlocking, then 50 percent unlocking at age 50 or over at the member's election should be the default.
- There should be no change to the existing rule that plans may disallow portability within 10 years before normal retirement.
- For transition purposes, individuals subject to the current Alberta legislation who are age 50 or over at the time the new legislation is enacted should be "grandfathered" under that rule regardless of the option selected for the plan going forward.
- There should be no change to the existing unlocking rules (subject to harmonization) with respect to:
 - shortened life expectancy;
 - non-residency in Canada; and
 - small amounts.
- Financial hardship unlocking should be applicable in both provinces using the Alberta model.

V. RELATED LEGAL AND OTHER FRAMEWORKS

INCOME TAX RULES

Recommendation 10.1-A The governments should actively advocate that the federal government change various tax rules that impact the pension system, including:

- raising the maximum contribution/benefit limits (to be more competitive with other major industrialized economies with which we compete for human resource talent)
- raising the maximum funding limits for DB plans to encourage more generous funding of such plans and improve benefit security, by allowing surpluses of up to 25 percent, except for Individual Pension Plans, where the current ten percent maximum excess would remain
- advocating any changes required to federal tax and bankruptcy and insolvency laws to support establishment of the Pension Security Fund
- updating the rules applicable to the maximum transfer values for DB to DC plans to allow larger amounts to be transferred tax-free
- making the tax rules flexible enough to accommodate new plan designs that meet the principles of general application under next-generation pension standards legislation
- allowing contributions by employees to broad-based plans to be deductible where their employer opts not to participate (See Sections 6.3 and 11)
- allowing self-employed individuals to make contributions to a registered pension plan

BANKRUPTCY AND INSOLVENCY ISSUES

Recommendation 10.4-A There should not be a pension benefit guarantee fund established in Alberta and British Columbia.

Recommendation 10.4-B The governments should encourage the federal government to extend the “super priority” secured creditor status to all due but unpaid contributions, including solvency deficiency or unfunded liability special payments, but not to extend such status to such amounts that are unamortized but not yet due.

Recommendation 10.4-C The governments should encourage the federal government to provide the PSF

with the same treatment under federal bankruptcy and insolvency legislation as applies to the regular pension fund of a pension plan. (See also Section 8.1.1 “DB funding rules” above.)

Recommendation 10.4-D The deemed trust rules in pension standards legislation need to be clarified to ensure that monies held for pension contributions are treated in the same manner as earned but unpaid wages under provincial employment standards legislation and, in situations other than bankruptcy, are not available to satisfy other creditors.

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VI. THE "ABC PLAN"

Recommendation 11-A The governments should establish a Steering Committee made up of experts in pension plan administration, governance and investment to examine the feasibility of establishing a multi-employer pension plan available to all employers and employees working in our provinces. The Steering Committee should have a mandate not only to make specific plan design recommendations but also to suggest the means by which key participants (especially employers and employees) in the ABC Plan operation would work together to ensure their buy-in to the ABC Plan's purposes and objectives. We also encourage the Steering Committee to consult with other provinces who may be considering similar plans.

Recommendation 11-B The ABC Plan design should be based on a simple DC formula with, generally, matching employer and employee contribution rates. Although the Panel recommends an entry level participation rate of a minimum of three percent of employee's earnings, the Plan design should be flexible enough to allow both employers and employees to make contributions without matching contributions from each other in order to encourage increased savings by all ABC Plan participants.

Recommendation 11-C All employers and workers, including self-employed individuals earning employment or self-employment income in either Alberta or British Columbia, should be eligible to participate in the Plan. All employers and employees should be automatically enrolled in the ABC Plan but the employer and/or their employees should be allowed to opt out of participation if they so choose. Employees whose employer has opted out should still be automatically enrolled without employer contributions unless they choose to opt out. Self-employed individuals in our provinces should also be encouraged to participate in the Plan. Auto-enrolment is not recommended – rather, participation by self-employed individuals should be on an opt-in basis.

Recommendation 11-F Governance of the ABC Plan should be at arm's length from government. There are several models of pension governance that the governments could consider.

Recommendation 11-H Administration of the Plan should be at arm's length from government. The board of governors would ultimately be responsible for deciding how best to structure the administration of the Plan.

Recommendation 11-I The Panel does not recommend that employers or employees contributing to the ABC Plan have any investment choice. Rather, the Panel recommends investment of the Plan assets would be subject to the policy direction of the board of governors.

Recommendation 11-J The Plan's design could include auto-annuitization, spreading out annuity purchases over time to minimize longevity risk and retirement end-date sensitivities which would help mitigate risks of market volatility.

Recommendation 11-L Contributions to the ABC Plan should be locked in similar to the locking-in rules applicable to any registered pension plan in our provinces.

Recommendation 11-M Vesting of employer contributions to the ABC Plan should be immediate.

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