



THE CANADIAN
BAR ASSOCIATION
L'ASSOCIATION DU
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POOLED REGISTERED PENSION PLANS

**NATIONAL PENSIONS AND BENEFITS LAW SECTION
CANADIAN BAR ASSOCIATION**

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PREFACE

The Canadian Bar Association is a national association representing 37,000 jurists, including lawyers, notaries, law teachers and students across Canada. The Association's primary objectives include improvement in the law and in the administration of justice.

This submission was prepared by the National Pensions and Benefits Law Section of the Canadian Bar Association, with assistance from the Legislation and Law Reform Directorate at the National Office. The submission has been reviewed by the Legislation and Law Reform Committee and approved as a public statement of the National Pensions and Benefits Law Section of the Canadian Bar Association.

TABLE OF CONTENTS

POOLED REGISTERED PENSION PLANS

I.	INTRODUCTION	1
II.	ISSUES FROM THE CONSULTATION PAPER	2
	A. INVESTMENTS AND COSTS OF INVESTMENTS	2
	B. AUTO-ENROLMENT.....	6
	C. ELIGIBLE ADMINISTRATORS.....	8
	D. ADMINISTRATION.....	10
	E. DISCLOSURE.....	12
	F. LOCKING-IN	13
	G. DUTY OF THE ADMINISTRATOR	13
	H. SUPERVISION.....	14
	I. HARMONIZATION	15
III.	ADDITIONAL ISSUES	16
IV.	CONCLUSION	16

POOLED REGISTERED PENSION PLANS

I. INTRODUCTION

The Canadian Bar Association's National Pensions and Benefits Law Section (CBA Section) is pleased to provide its views concerning the Pooled Registered Pension Plans (PRPPs) initiative of Finance Canada. The CBA Section's members are involved in pensions and benefits law across the country, including as counsel to pension and benefit administrators, employers, unions, employees and employee groups, trust and insurance companies, pension and benefit consultants, and investment managers and advisors.

The CBA Section welcomes this initiative to explore new retirement savings vehicles for Canadians. The *Framework for Pooled Registered Pension Plans*, released by Finance Canada in December 2010, states that PRPPs would improve the retirement savings system by providing an "accessible, straightforward and administratively low-cost retirement option", particularly for the self-employed and employees of small and medium sized businesses who currently do not participate in registered pension plans (RPPs). PRPPs are held out as "ensuring that funds are invested in the best interest of plan members" and having "lower investment management costs" resulting from membership in a large pooled pension plan.

The CBA Section believes that PRPPs have potential to increase pension coverage and retirement savings for Canadians, but only if the advantages outlined by Finance Canada are realized through the design and implementation of a carefully constructed regulatory regime.

Prior to the CBA Section's meeting with government representatives in February 2011, we considered the questions in Finance Canada's consultation paper. Some of those questions are beyond the range of expertise or the mandate of the CBA Section. The CBA Section has addressed those questions on which we can offer a positive contribution. For ease of reference, the questions are answered in the same order as in the Finance Canada consultation paper.

II. ISSUES FROM THE CONSULTATION PAPER

A. INVESTMENTS AND COSTS OF INVESTMENTS

According to the framework document agreed to by Federal/Provincial/Territorial Ministers of Finance, PRPPs will result in large pools of capital with low costs, while helping members to construct portfolios consistent with each member's particular investment needs and objectives. Members will be able to choose from a suitable low-cost option intended for a broad group, as well as a manageable number of other investment options. The design of appropriate default funds where members do not make an investment choice is also a key consideration.

1. How should the framework address the number of investment choices offered by an administrator?

- **What would be an optimal number of investment choices that an administrator should offer? What types of funds should be offered at a minimum (i.e. type of assets in the funds)?**

The rules governing the investment choices and the type of funds available under the PRPPs should be harmonized with existing rules applicable to capital accumulation retirement and pension plans in Canada, including the Capital Accumulation Plans Guidelines adopted by CAPSA (Cap Guidelines). Pension Benefits Standards Act (PBSA) (Canada) regulations supporting new sections 8(4.2), (4.3) and (4.4) may also contain guidance and, if so, should be considered for harmonization purposes.

- **How should this optimal number be determined (e.g., By the administrator? Prescribed in regulation?)**

The optimal number of funds may vary depending on the group's characteristics e.g. a group of financially literate members could have more options. It would not be possible to determine an optimal number of funds by regulation, although a minimum number could be required as is already the case under some pension laws and the Cap Guidelines.

The standard should be expressed to the effect that the PRPP administrator "[...] must offer investment options of varying degrees of risk and expected return that would allow a

reasonable and prudent person to create a portfolio of investments that is well adapted to their retirement needs.”¹

2. According to the Framework Document, PRPPs are large pools of capital with “low costs”

- **What should be included in the definition of costs? Can these costs be disaggregated on a comparable basis?**

The CBA Section emphasizes the importance of transparency in disclosing costs. Fees must be in a form that is easily understood and compared by employers and plan members. To achieve this result, there should be a government designed standard form for disclosure of all fees, commissions and other compensation (i.e., all administrative and investment costs should be presented “unbundled” to ensure greater transparency and understanding). This form should be filed with the regulator and available to all members of the public on a website. The website should also contain information on how these costs compare to administrative and investment costs incurred by other types of plans, such as plans for public sector and quasi-public sector employees, the Canada Pension Plan and, perhaps, some international comparators.

- **What are the drivers of cost?**

No comment.

- **Plan Administrators and Investment Managers: How does the provision and cost of investment/financial advice to plan members fit into the costs?**

No comment.

- **Should “low cost” (i.e. as it relates to the PRPPs in general) be defined in the framework?**

No comment.

- **Is there a particular threshold at which a cost is no longer low?**

While there may be no single threshold, where fees are comparable to other substitute products (unit costs in RRSPs, DC and DB plans), they may serve as a guide to competitive pricing. Moreover, the CBA Section recommends that the fee structure, or acceptable range of fees, be provided by regulation.

¹ See language used in federal Bill C-47, section 183 adding section 8(4.3) to the *PBSA* (Canada).

- **Should there be a limit on fees for the low cost investment option?**

No comment.

3. The framework document notes that the investment options should specifically include “a low cost option.”

- **In this context, how should “low cost” be defined in the framework? Should there be a fee limit?**

See comments above under question 2.

- **How should this low cost be operationalized (e.g. Rule-based approach? Principle-based approach)?**

No comment.

- ***Plan Administrators and Investment Managers:* What are the 3 lowest-cost actively-managed and 3 lowest cost passively-managed funds you offer? How do you demonstrate the value of higher cost funds?**

No comment.

4. The Framework Document notes that “there will be a suitable low-cost default option for a broad group(that) will be permitted to have some risk exposure and still be considered prudent under this framework for the purpose of the fiduciary duty.”

- **Should a "safe harbour" provision be implemented and, if so, how should it be designed?**

Canadian plan sponsors are concerned with costly lawsuits involving pension plans, and would be comforted by the existence of a safe harbour for PRPPs. However, plan members may view a safe harbour protection as unjustly and unnecessarily limiting their rights of action against plan sponsors or administrators if losses are legitimately attributable to administrator actions or omissions. As the CBA Section represents a wide range of interests, we have no position on this issue.

- **Should there be certain “qualified” investment for default options or should general parameters be set for establishing default options as prudent. If the latter, what types of parameters should be considered?**

The CBA Section believes that a plan sponsor or administrator must provide a default investment option. Some factors involved in selecting a default option are:

- the availability of the option from the provider (all providers do not currently provide target date funds);

- the management expense ratio of the option (as compared to other options made available);
- the sophistication of the work (the ability to understand the risks and rewards of the option);
- the ability and cost for members who wish to switch options;
- whether investment education and investment advice is provided; and
- the level of required and optional member contributions.

The plan sponsor or administrator should communicate the risks and rewards of the default option both initially and periodically, with realistic return projections, in terms understandable to plan members.

Accordingly, the CBA Section would be concerned with legislation requiring a specific type of default option (i.e. a balanced fund, a target date fund or a GIC) rather than a checklist of matters required to be taken into consideration in selecting a default option. However, the legislation should expressly require a default fund and provide criteria that must be taken into account when establishing the default fund. Emphasis should be placed on the information and the periodic communication that must be provided to participants regarding the consequences of relying on a default option that might or might not be appropriate for them.

Also, decision-making tools (e.g. investor profile questionnaire, retirement income projection) should be available for participants to assist in their investment decisions.

- **What do you consider to be a prudent level of risk exposure?**

This question is not possible to answer in any generic sense. Risk exposure may vary with the participant and with the plan design.

- **Plan Administrators: Do you presently offer lifecycle funds? What does it cost, and what are the major drivers of cost. What is the lowest cost life-cycle-type fund that could be designed?**

No comment.

5. How should the default investment strategy be chosen?

- **How much and what kind of diversification should be required in the default fund?**

Please see comments under question 4.

- **Should multiple default options be offered based on contributor's age or risk tolerance?**

Please see comments under question 4.

- **How would the risk balance be adjusted over time as a contributor ages?**

Please see comments under question 4.

B. AUTO-ENROLMENT

An employer that chooses to offer a PRPP will enroll its employees (or certain classes thereof) into the plan it has chosen. Employers may be permitted to enroll their employees into a PRPP during the tenure of the employee's employment, and not only at the hiring stage.

- 6. Should employers be permitted to enrol existing employees into a PRPP (i.e., not simply at the hiring stage)? If so, should the employee be required to consent or have the ability to opt out?**

Given the government's goal to reach a broader pension "audience", employers should be able to enroll existing employees into a PRPP without express consent, provided employees are able to opt out. This may require amendments to provincial employment standards legislation, particularly those requiring written employee consent for deductions from salary or wages.

- 7. If able to opt out, how should an opt-out be structured for employees that are automatically enrolled into a PRPP?**

Any opt-out should be structured as simply as possible, to allow employees to easily opt-out with no penalty or tax consequences. However, it should also be structured in a way that reduces administrative burdens for the administrator and/or plan sponsor.

- **Should there be a certain period of time following enrolment that opt-out would be permitted?**

Opting-out should be permitted at all times.

- **How should contributions be treated when individual opts-out (e.g. market rates? protected?)**

If the goal for PRPPs is simplicity, low cost and to encourage retirement savings, then all amounts contributed to a PRPP should be locked-in (and subject to existing rules on locking-in under the *Income Tax Act* and existing pension legislation). If the funds are not locked-in, the administrative complexity and tax ramifications that ensue could increase the cost of the PRPP.

8. Should employer participation be mandatory unless the employer already sponsors an RPP?

The government has engaged in the PRPP discussion because of concerns about the inadequacy of pension coverage in Canada. Mandatory employer participation (although this would not necessarily mean mandatory employer contributions) would ensure that the PRPP is available to all Canadians who may not have had a previous opportunity to participate in a pension plan. It also ensures that larger pools of funds are available to keep costs lower. However, if auto-enrolment is also adopted, see comments under question 6 on necessary changes to employment standards legislation to address deductions from salary and wages.

9. How should default contribution rates be set for member auto-enrolment and who should set the contribution rates?

The same approach as for the default option should be taken for the default contribution rate.

Please see comments under question 4.

- **Should all members have the same default contribution rate, or should it vary by age, tenure or other factor?**

Please see comments under question 4.

- **What criteria should be used to set contribution rates?**

Please see comments under question 4.

- **What is the relationship between default contribution rates and the rate at which people opt out of pension plans in other jurisdictions?**

No comment.

- **Should members be offered additional financial information if they want to change their contribution rate?**

Information is essential in capital accumulation plans at all stages.

10. Should the automatic escalation of contributions over time form part of the PRPP framework? If so, what factors should determine the extent of the auto-escalation?

Automatic escalation would help achieve the objectives of PRPP, but an individual should have the ability to opt out of the escalation. Escalation could be tied to certain life or employment events (e.g. promotion), or set at certain time periods, with specified incremental increases tied to those events to a maximum percentage of salary. In any event, the mechanism and its consequences should be simple and well communicated to employees.

11. What would be the responsibilities and requirements of an employer that does not contribute to the proposed plan (duty to inform employees, providing the plan if a sufficient number of employees request it, choice of plan, terms and conditions, payroll deductions)?

Even if the employer does not contribute, the employer would select the PRPP administrator, ensure that auto-enrolment and auto-escalation occur, remit contributions to the administrator, notify the administrator of any plan member changes, and assist the administrator by ensuring that communications materials concerning the plan are distributed in the workplace.

Given the range of views within the CBA Section, we have no position on the nature and level of responsibilities. However, the CBA Section recommends that the duties of both the plan sponsor and the administrator be clearly identified in specific terms.

12. Is there a practical way to avoid the multiplication of accounts caused by employees changing jobs?

No comment.

C. ELIGIBLE ADMINISTRATORS

Regulated financial institutions that are capable of taking on a fiduciary role will be eligible administrators of PRPPs.

13. Should there be further restrictions on eligible administrators (e.g. capable of offering a plan in multiple jurisdictions; experience)?

If PRPPs are offered by regulated financial institutions capable of taking on a role similar to that of an "administrator", then additional restrictions would seem unnecessary. The market will ensure that PRPP administrators remain competitive (e.g. if a qualified administrator cannot offer a plan in multiple jurisdictions, it will have to change to remain competitive). If non-financial institutions offer the product, then the standards for all should be the same.

The smaller the group of eligible administrators, the less likely there will be a price-competitive functioning market. A more diverse group of eligible administrators and eligible sponsors, and a more diverse set of terms upon which they can create a PRPP, would likely be necessary to ensure appropriate fee arrangements.

14. How should a PRPP be constituted legally (e.g., as an insurance contract or trust agreement)?

Both examples could work. The choice should be left to the sponsor and administrator.

15. Are there means through which companies, other than trust companies, could take on a fiduciary duty to plan members?

If PRPP administrators are subject to provincial pension standards, then those standards would apply in the same manner and to the same extent as they do to RPPs.

However, the CBA Section has not reached a consensus on the nature and level of responsibilities appropriate to impose on administrators of PRPPs. In the Framework, where administrators are third party financial institutions remunerated for services rendered and their compensation could be affected by the choice of investments, it would be difficult to reconcile that role with a fiduciary obligation towards member that would include acting in their best interest (e.g. charging the lowest costs possible).

The CBA Section recommends that the duties of the administrator be clearly identified in specific terms, rather than only by a reference to a general obligation such as a fiduciary duty or a duty of care.

16. How would the nature of the contract or relationship between administrators and members differ based on the type of eligible administrator (e.g., trust agreement, insurance contract)?

The nature of the relationship should be the same. The nature and level of responsibilities should not depend on the type of administrator. See comments under question 15.

17. To encourage competition between plan administrators, should there be terms that enable employers to change plan administrators? If so, what should these be?

Employers should be able to change plan administrators without too many administrative and legal restrictions. The terms of administrative arrangements may include a required clause that permits employers to terminate participation and transfer administration (and account values) to other registered PRPPs on reasonable notice.

D. ADMINISTRATION

18. How should funds be paid out at retirement?

Members should be able to transfer account values between PRPPs and RPPs and other locked-in arrangements in accordance with current portability rules in pension legislation. All contributions should be locked-in. Forms of benefits permitted by PRPPs should include:

- **annuitization or auto-annuitization over time;**
- **transfer to locked-in arrangements; and**
- **“target benefit” designs that can be adjusted up or down according to fund experience.**

19. What types of products (e.g., annuities, RRIFs, lump sum payments) would you recommend to reduce the risks and costs of converting members' plan balances to a secure stream of retirement income?

See comments under question 18.

20. Should members have to transfer assets out of their plan at retirement to a disbursement vehicle, or should the plan be permitted to continue to hold and invest their money, and then pay income out in LIF-like payments?

No comment.

21. What regulatory changes might be required to support flexible de-accumulation options at retirement?

Transfer options and payment of benefits options at retirement should use vehicles already existing in pension legislation. Regulatory changes would be minimal, avoiding having to introduce new concepts and vehicles not well understood by participants.

22. How could plans make it easier for their members to understand the decisions they need to make at retirement regarding the conversion of their plan assets into an income stream?

It would be easier for members to understand the decision they need to make if they have access to clear plan provisions and easily accessible information.

23. Could professional, business or sector associations be able to sponsor a plan on behalf of their members?

PRPPs are intended to appeal to small and medium size employers who cannot participate in defined contribution (DC) plans, self-employed persons, and other persons who do not have access to either a RPP or other retirement savings vehicle. This is an appropriate target group, but it should be expanded to include associations of professionals and other self-employed

individuals. These groups often have fairly high incomes and could use a more efficient savings retirement system than RRSPs. These groups would probably be the largest single sub-group of users of PRPPs.

- **What are the potential benefits of having organizations act as a sponsor on behalf of a large group of individual members?**

They can promote retirement savings through access to a lower cost option for retirement savings than currently available.

- **What particular responsibilities, apart from plan selection, would sponsors have that would be distinct from plan administrators?**

The employer would select the PRPP administrator, determine whether it (i.e. the employer) will make contributions to the plan, ensure that auto-enrolment and auto-escalation occur and remit contributions to the administrator, notify the administrator of any plan member changes, and assist the administrator by ensuring that communications materials concerning the plan are distributed in the workplace.

As to the nature and level of responsibilities, again the CBA Section has not reached a consensus on those issues. However, the CBA Section recommends that the duties and responsibilities of the plan sponsor and administrator be clearly identified in specific (rather than general) terms. The standardization of those roles would lead to a standardization of plan terms, and added clarity, ease of administration and lower costs could be achieved.

24. Should there be provisions to ensure that employers, both large and small, and self-employed workers can take advantage of the same plan subscription terms (for example, management fees)?

Each provider should have standard plan terms and standard fees available to all employers, both large and small, and self-employed workers. Negotiation of plan terms and fees adds to the cost of the plans for all, first due to the costs of negotiations and second since customized terms add to administrative complexity. Moreover, if this were not the case, smaller employers would be unlikely to be able to negotiate the lowest rates. As a primary driver of the PRPP proposal is the potential to attract small employers and the self-employed to a straightforward, low cost plan, having the same terms and fees for all is an essential requirement.

The Framework suggests that lower investment management costs will result from membership in a large pooled pension plan. Steps must be taken to ensure that this is in fact the case, such as providing by regulation the fee structure. Plan terms should be filed with the

regulator. The regulator should review the plan terms to ensure compliance with the legislation.

25. How do financial institutions intend to use their current distribution system to promote the PRPP?

No comment.

- **With that in mind, how do they plan to reduce distribution costs, which currently account for a large percentage of the total management fees?**

No comment.

E. DISCLOSURE

Plain language disclosure of plan provisions and investment performance is critical for members to understand the nature of their participation in PRPPs.

26. Are the disclosure requirements contemplated in the framework appropriate?

The CBA Section agrees that disclosure of plan provisions, investment performance (and fees) is critical for members to understand the nature of their participation.

We urge the government to adopt a principles-based approach to issues such as this. For example, for disclosure, the principles of transparency and clarity should be the expected standards, as opposed to a defined “laundry list” of items that may require amendments as time progresses.

27. What degree of detail should be disclosed on costs and fees? How should this be operationalized?

No comment.

- **Can these costs be compared across funds?**

No comment.

- **Follow up to Plan Administrators: To what extent are these the same as in the CSA’s Fund Facts?**

No comment.

F. LOCKING-IN

Employer contributions will be locked-in. Some jurisdictions may allow employees to choose that their contributions not be locked-in. However, what is locked-in would follow each jurisdiction's rules for locked-in funds (e.g., small amounts, financial hardship).

28. Should employee contributions be locked-in? Are there situations in which unlocking of contributions prior to retirement should be permitted?

In our view, employee contributions should be locked-in subject to the same exceptions under pension legislation (small amount, financial hardship, life expectancy).

G. DUTY OF THE ADMINISTRATOR

- **In order to protect the interests of plan members, the administrator will have a fiduciary duty to plan members.**

On the one hand, imposing a fiduciary standard may make it difficult or impossible for commercial enterprises to deliver PRPPs. A more appropriate standard of care should be implemented to require that those delivering PRPPs act with prudence, diligence and treat participants fairly. On the other hand, when an administrator administers money on behalf of a PRPP member, it could be concluded that the appropriate standard of care is that of a fiduciary, which requires the use of skills, care and diligence that a prudent investor or prudent person would use in the management of property of others. The responsibilities and duties of an administrator should then be those found in provincial pension legislation.

Although the CBA Section has not reached a consensus on the nature of those responsibilities, it strongly recommends that the responsibilities of both the employer and the administrator be clearly detailed in specific terms in the legislation to reduce exposure to the risk of litigation. The role and responsibilities of participants should also be clearly communicated to them (e.g. level of contributions, investment decisions).

The CBA Section also recommends that the government thoroughly examine the level of exposure to liabilities of the various stakeholders (i.e. administrators, employers and employees). The CBA Section believes that it is important to balance the responsibilities of all stakeholders while also ensuring that the objectives of PRPPs are met, including the impact on possible fees and the protection of members.

29. How should the duty of the administrator be designed in order to protect plan members and at the same time limit the costs imposed on the administrator?

Although the CBA Section has not reached a consensus on the nature of responsibilities, we recommend that the responsibilities of both the employer and the administrator be clearly detailed in the legislation to reduce exposure to the risk of litigation.

- **What specific requirements or limitations should be placed on the administrator in order to protect the interests of plan members?**

Again, although the CBA Section has not reached a consensus on the nature of the administrator's responsibilities, we recommend that the responsibilities of both the employer and the administrator be clearly detailed in the legislation to reduce exposure to the risk of litigation.

- **Plan members could also be protected through the role of the supervisor or an independent board of trustees.**

There is no need for another layer of monitoring. However, PRPPs should be regulated and monitored by existing pension regulators.

30. What are the advantages and disadvantages of the different approaches?

Please see comments above.

H. SUPERVISION

Proper supervision of the administration of PRPPs would be required.

31. What should be the role of the supervisor?

PRPPs would be provincially regulated. The role of the supervisor (the regulatory authority) should be the same as with any other RPP.

However, we recommend that the federal government take the lead in pressing for harmonized legislation and regulations for PRPPs, common to all, with little room for jurisdictional variations.

32. What should be the nexus between the role of the supervisor and the role of the administrator?

They both have a very different role, as it is already the case with RPPs.

- **What level of supervision should be required?**

The level should be the same as with other RPPs.

- **How much should the administrator be relied upon to adhere to the requirements under the framework?**

Administrators should not have much latitude in that respect.

33. Given that PRPPs will be offered across the jurisdictions in Canada, how should the supervisory framework be structured in order to be most effective?

- **Would it be effective to follow the multilateral agreement approach² being enacted for RPPs?**

PRPPs will be supervised at the provincial level. The CBA Section recommends that the multilateral agreement approach be followed.

I. HARMONIZATION

A high level of regulatory harmonization across the federal, provincial and territorial governments will be instrumental in increasing the scale of these plans and achieving low costs.

34. What design elements of the framework are most important to be harmonized and to what degree?

From our understanding, there are the three options to implement PRPPs:

- **Creating a new statutory framework which would apply only to PRPPs that would require adoption at the provincial, territorial and federal level and that would likely be developed through a model law or a multilateral agreement and framework.**
- **Create an interprovincial/territorial agreement on the basic features of PRPPs that would then be introduced into existing legislative frameworks (pension legislation and income tax legislation). That agreement would have the effect of incorporating a number of existing rules and regulations that apply to pension plans, and create a new category of plan under the existing rules.**
- **Leave discretion to each province and territory to create its own PRPP rules based on the PRPP framework.**

The CBA Section recommends that the federal government take the lead in pressing for harmonized legislation and regulations.

² Under this approach, the lead regulator of a PRPP would be the major authority, which would be the jurisdiction where the plurality of members is located. The lead regulator's framework would apply for all 'plan related' matters, while other rules would apply for matters more related to the individual member, such as disclosure and locking-in requirements.

35. How will harmonization impact size, scale and costs of PRPPs?

This goes to the goal of keeping the product simple and the costs low. A lack of harmonization would lead to a decline of both, while full harmonization would further simplify the product and reduce the costs.

III. ADDITIONAL ISSUES

36. Does the Bar Association have a view on the appropriate standard of care (e.g. fiduciary vs. good faith? Do you have any suggestions for a detailed model in this respect (i.e. specific language)?

37. How would you propose to specifically set out the responsibilities/duties of the administrator in statute?

Please see comments under question 28.

IV. CONCLUSION

The CBA National Pensions and Benefits Law Section trusts that our comments will assist Finance Canada in its work on this important initiative. We would be pleased to respond to questions and to provide further information regarding any of the issues we have addressed in this submission.