THE CANADIAN BAR ASSOCIATION
L'ASSOCIATION DU BARREAU CANADIEN

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Via email: pensionreg@novascotia.ca

Paula Boyd
Superintendent of Pensions
Finance and Treasury Board
Pension Regulation Division
PO Box 2531
Halifax, NS B3J 3N5

Dear Ms. Boyd:

Re: Pension Funding Framework Review and other issues affecting pension plans

The Canadian Bar Association Pensions and Benefits Law Section (CBA Section) is pleased to comment on the Nova Scotia Department of Finance and Treasury Board (NS Finance) discussion paper, *Pension Funding Framework Review and other issues affecting pension plans* (the Discussion Paper).

The CBA is a national association of over 36,000 members, including lawyers, notaries, academics and students across Canada, with a mandate to seek improvements in the law and the administration of justice. The CBA Section contributes to national policy, reviews developing pensions and benefits legislation and promotes harmonization. Our members are involved in all aspects of pensions and benefits law, including counsel who advise pension and benefit plan administrators, employers, unions, employees and employee groups, trust and insurance companies, pension and benefit consultants, and investment managers and advisors.

Harmonization

The CBA Section has long advocated for harmonization of pension legislation across Canada.[1] Our comments are informed by this perspective.

Part 1: Framework for Defined Benefit Pension Plans

The CBA Section does not take a position on policy issues engaged in the Discussion Paper but advocates three values in considering potential changes to the funding model:

1. Sustainability – robustness with respect to changing economic conditions;
2. Clarity – legislative guidance on entitlements to and uses of plan funds; and

[1] See for example, Canadian Bar Association, *Resolution 10-01-M Harmonization of Pension Laws* (February 13-14, 2010), available online (http://ow.ly/7pco30gHA9Z).

3. Harmonization – alignment with rules in provinces that have already undergone solvency funding reform.

When weighing between proposed funding models, NS Finance would be well served by promoting these values as much as possible in the circumstances.

Sustainability

As noted in the Discussion Paper, solvency funding relief has been introduced on a periodic basis since the 2007-2008 market downturn. Long term interest rates have since been chronically low, weakening plans' solvency positions. Responses to date for specific plans or classes of plans have been made on an ad-hoc and reactive basis.

The CBA Section believes it is important that a new solvency funding framework (if any) be designed to be manageable in the long term, and fair and equitable to all stakeholders in all economic environments. Further, there should be sufficient flexibility in the solvency funding regime to provide the necessary counterbalances to economic shifts.

The CBA Section suggests a more unified and consistent funding framework. In our view, this would contribute to significant progress in meeting the goal of sustainability through promoting predictability of future funding requirements and could also address the concerns of contribution volatility.

Clarity

In connection with any changes proposed to the current solvency funding framework, greater clarity should be provided on the potential uses of and entitlement to the funds (including, but not limited to, any other methods of funding and/or addressing plans in a deficiency position, such as the proposed solvency reserve accounts and/or letters of credit).

Harmonization

We highlight the need for and the inherent fairness in having rules across Canadian jurisdictions that are as harmonized as possible, particularly on funding.

As noted in the Discussion Paper, recent reforms to solvency funding have been markedly different across different Canadian jurisdictions:

- The approach in Alberta and British Columbia preserves solvency funding requirements, but provides for solvency reserve accounts to allow withdrawal of funds if certain conditions are met.
- Québec, on the other hand, has recently eliminated the requirement for solvency funding for most ongoing plans altogether, albeit with the corollary introduction of a new stabilization provision as well as accompanying changes to the rules governing portability and surplus rights.
- Ontario has announced that it will essentially eliminate the solvency funding requirement for defined benefit plans provided the plans maintain at least an 85% funding ratio. This will be coupled with a new requirement to establish a funding reserve within the plan and a shortened amortization period for funding a shortfall.

Should Nova Scotia's rules deviate from these approaches it would further exacerbate this patchwork of funding rules.

CAPSA is working towards a new agreement for 2018 that is intended to harmonize, among other things, funding rules for multi-jurisdictional plans. Adopting a distinct solvency funding framework that applies for Nova Scotia-registered plans would further complicate the implementation of an agreement.

Part 2: Regulatory Issues

A. Target Benefit Plans

1. Should Nova Scotia proceed with developing a regulatory framework for target benefit pension plans?

Despite the addition of a variety of forms of target benefit plan provisions in a number of pension standards statutes across the country, there remains a lack of consensus among pension professionals as to whether they are desirable or beneficial in the single employer or public plan context. Defined benefit (DB) pension plans remain prevalent, particularly in the public sector.

Members of the CBA Section have differing views on target benefit plans. On the one hand, some members believe target benefit plans reduce benefit security and shift risk onto plan members. These members have concerns with certain key features of target benefit plans, namely the absence of an employer deficit funding obligation, and an ability to reduce benefits (and sometimes accrued benefits) – with potentially lesser benefits in that context.

On the other hand, other members of the CBA Section believe there is a recognition that a target benefit plan model may be more desirable and provide greater retirement income security and adequacy relative to the defined contribution (DC) plan model and existing DB models that have been terminated with insufficient assets to provide for the benefits set out in the plan. Some members of the CBA Section also believe the target benefit plan offers greater predictability of both benefits and contributions than other plan models; pooling of longevity and investment risks; and flexibility of plan design to enhance sustainability. Moreover, the target benefit plan is generally an acceptable middle ground in truly strained financial circumstances where the DB plan is in jeopardy of being eliminated.

Given these differing views among the CBA members, it is not possible to fully support the development of a target benefit plan regulatory framework that would be available to supplant DB pension plans.

In the multi-employer pension plan (MEPP) context, of course, target benefits have long been, including from inception, an accepted and acceptable feature of those plans. By their very nature, the fact that contributions are negotiated and fixed, the ability to vary benefits is essential to their long term viability. That is, where the 'promise' to plan members and retirees is known and understood from the outset not to be a guarantee of a particular level of benefit – members know that their benefits are ultimately vulnerable to market volatility and poor experience. Thus, where the nature of the target benefit is known and clearly understood by members, target benefits are uncontroversial in MEPPs and an accepted part of that type of pension plan. To the extent NS Finance is asking about the clarification of target benefits in MEPPs, and MEPPs as target benefit plans, the CBA Section is fully supportive.

2. Should target benefit pension plans be restricted to unionized environments?

The CBA Section has differing views on this question. Some members of the CBA Section see some advantages to the availability of target benefit plans in unionized workplaces, particularly in

circumstances where the status quo is a DB pension plan and the employer is seeking to replace it with a target benefit plan. If negotiation of the implementation of a target benefit plan is required by the applicable legislation, members of the plan can at least be assured a voice in the process through their union. With the appropriate level of disclosure and information, members will have a real opportunity to understand and appreciate – and of course to have input into - the changes being suggested.

Some members of the CBA Section are of the view that the existence of a bargaining agent with resources and bargaining strength will ensure that the members' interests are paramount in the determination of whether a target benefit plan is put in place at all, and if so, its design and level of funding, which will greatly impact the delivery of a secure and adequate retirement income benefit.

On the other hand, other members of the CBA Section believe that target benefit plans should be open to non-unionized employees and workplaces and could be valuable in the non-unionized context. Issues faced by DB pension plans in unionized workplaces also apply to non-unionized workplaces. Issues of negotiation, disclosure, resources and informed consent would need to be addressed in the context of a target benefit plan in the non-unionized workplace through mechanisms other than the bargaining agent.

3. Should defined benefit plans be permitted to convert to target benefit plans, including benefits earned in the past?

Thus far, in the short evolution of target benefit plans in Canada, the availability of conversion of defined benefits (especially the conversion of accrued benefits) is highly controversial and has been the subject of multiple challenges, including constitutional challenges. There has yet to be a model proposed or implemented that is free from opposition or potential for challenge. This potential is elevated to a high degree where there is a possibility of converting accrued benefits, making them subject to possible reduction. The CBA Section also has differing views, which we share below.

In the view of some members of the CBA Section, the ability to convert earned benefits from a guaranteed benefit to one contingent on appropriate levels of funding is unsupportable. It is inconsistent with one of the purposes of pension standards legislation – protecting accrued benefits. The hallmark of DB plan benefits is the sanctity of the promise and pension standards legislation has long been its protector, not permitting those earned benefits to be reduced, and providing that amendments with the effect of reducing accrued benefits are void ab initio.

Some would argue that accrued defined benefits have already been paid for by members and pensioners through their work – the members have delivered their end of the bargain, it is objectionable to reduce compensation that was already agreed-on and for which services were rendered.

Other members of the CBA Section believe that, with informed consent, proper safeguards, and in certain circumstances, the conversion of accrued benefit to target benefits should be permitted. In some cases, these arrangements have been the only option to maintain the defined benefit structure while ensuring that the plan is not underfunded in the long term, and that benefits are paid according to the funds available. The bar for converting accrued defined benefits must, however, be set very high.

While the bar would need to be very high for conversion, the view of these members of the CBA Section is that, if the legislative goal is to facilitate conversion of accrued benefits other than by a unilateral action of a DB plan sponsor, conversions should be able to proceed with informed consent where members could choose to convert their own accrued benefits. Unanimous consent

would not be required. Where active members are represented by a union, the union could consent on behalf of active members. In the case of retirees and non-unionized employees, consent could be obtained individually. The CBA Section also suggests that any requirement to obtain consent from active members and retirees with significant accrued benefits be polled separately from those without.

B. Annuity Discharge

Many DB plan sponsors consider purchasing annuities as part of a de-risking strategy, an option which clearly benefits the associated member. However, under the current legislation and case law, DB plan sponsors are left with a residual liability to those members, notwithstanding the annuity purchased. The CBA Section supports the notion of giving a statutory release from liability for administrators or sponsors who purchase an annuity for a benefit entitlement payable under a DB provision of a registered pension plan. British Columbia already provides a statutory release of this nature: section 89.1 of the British Columbia *Pension Benefits Standards Act*, along with section 83 of the associated regulations gives guidance on this issue and is a possible precedent.

The CBA Section also recommends that any statutory amendment allowing for a release from liability apply to annuities purchased in the past that meet the requirements of the legislation. Some plan sponsors may not be aware of the potential residual liability notwithstanding the purchase of an annuity. Further, the policy rationale for encouraging annuity purchases going forward also applies to the annuities purchased in the past.

C. Permitted Investments

The investment of pension plan assets is an important aspect of plan administration. A balanced approach is necessary in regulating pension investment to protect the interests of plan beneficiaries while giving flexibility in administering and investing plan assets. The CBA Section believes the existing requirements established under the Federal *Pension Benefits Standards Act* and its regulations as they govern the investment of plan assets are sufficient to protect the interest of beneficiaries. Similarly, they maintain sufficient flexibility for the administration and investment of plan assets.

The CBA Section's position on harmonization of pension legislation also applies to the investment rules. In response to Discussion Questions 12 and 13, the permitted investment rules should mirror those established federally, ideally by repealing and replacing the current investment rules with reference to the federal Pension Benefits Regulations. We do not foresee any situation where it would be important to have different rules for Nova Scotia pension plans in relation to permitted investments.

The CBA Section appreciates the opportunity to comment on the Discussion Paper. We trust that our comments are helpful and would be pleased to provide any further clarification.

Yours truly,

(original letter signed by Gillian Carter for Elizabeth Brown)

Elizabeth Brown
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Cc: Ms. M. Jean Beeler, CBA Nova Scotia Branch President (jbeeler@weldonmcinnis.ca)