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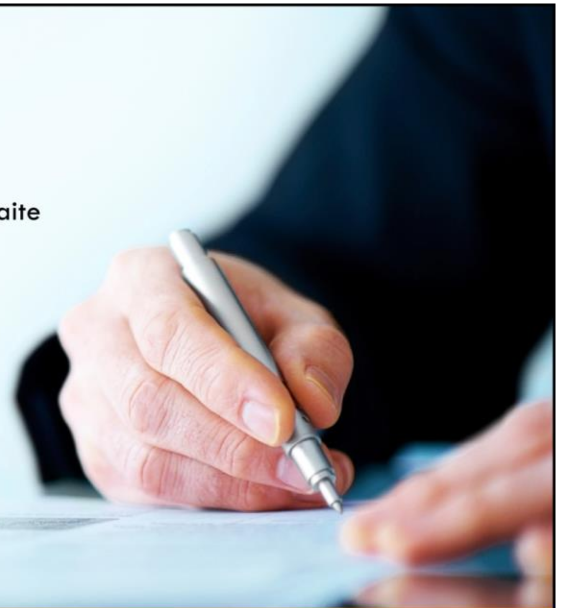

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ACPM Response to the Proposed Ontario Regulations to Facilitate the Merger of BPS SEPPs with Existing JSPPs or Conversion to New JSPPs

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FOREWORD

THE ASSOCIATION OF CANADIAN PENSION MANAGEMENT (ACPM)

ACPM is a national non-profit volunteer-based organization acting as the informed voice of plan sponsors, administrators and their service providers, advocating for improvement to the Canadian retirement income system. Our membership represents over 400 retirement income plans consisting of more than 3 million plan members, with assets under management in excess of $330 billion.

ACPM believes in the following principles as the basis for its policy development in support of an effective and sustainable Canadian retirement income system:

Diversification through Voluntary / Mandatory and Public / Private Options

Canada's retirement income system should be comprised of an appropriate mix of voluntary Third Pillar and mandatory First and Second Pillar components.

Third Pillar Coverage

Third Pillar retirement income plan coverage should be encouraged and play a meaningful ongoing role in Canada's retirement income system.

Adequacy and Security

The components of Canada's retirement income system should collectively enable Canadians to receive adequate and secure retirement incomes.

Affordability

The components of Canada's retirement income system should be affordable for both employers and employees.

Innovation in Plan Design

Canada's retirement income system should encourage and permit innovation in Third Pillar plan design.

Adaptability

Canada's retirement income system should be able to adapt to changing circumstances without the need for comprehensive legislative change.

Harmonization

Canada's pension legislation should be harmonized.

Introduction

We are pleased to provide ACPM's comments on the proposed content of the Regulations under the *Pension Benefits Act* (Ontario) (the "PBA") to facilitate the merger of Ontario broader public sector (BPS) single employer pension plans (SEPPs) with existing jointly sponsored plans (JSPPs) or conversions to new JSPPs. We generally support the Government's efforts to create a framework to permit voluntary mergers and conversions to JSPPs, both in respect of BPS and private sector pension plans.

In reviewing the proposed content of the proposed Regulations, we have not only considered how these rules would be applied to BPS SEPPs considering merging with or converting to a JSPP, but also how they would apply to private sector SEPPs should similar rules be implemented in respect of those plans in the future. Our comments and recommendations relating to the proposed Regulations are outlined below.

1. Notice of Proposed Merger or Conversion to Plan Beneficiaries

The proposed Regulations outline the information to be included in the notices to plan beneficiaries, including a "statement that members or their representatives would have a role in making decisions about the terms and conditions of the pension plan when they become members of the JSPP". ACPM recommends that this required statement be deleted as it is misleading considering many JSPPs have governance structures that do not permit all members or their representatives to have decision-making roles. Instead, the description of the joint governance structure of the JSPP (also required to be included in the notice) should suffice in this regard as it will describe how decisions are made.

2. Consent for Plan Beneficiaries and Trade Unions to Proposed Plan Merger or Conversion

The proposed Regulation suggests the following consent requirements for both a plan merger and a conversion:

- two-thirds consent from members; and
- no more than one-third of retired members, former members and other plan beneficiaries, as a group, object.

In ACPM's view, rules permitting mergers and conversions to JSPPs should be based on the one-third of affected member objection standard. There is precedent for this approach in the rules applicable to surplus sharing and solvency relief. Requiring two-thirds positive active member consent to a merger or conversion would be entirely impractical, rendering many impossible to implement.

The ACPM recommends that the "opting out" approach be adopted based on a one-third of affected beneficiary objection standard. That is, to block a merger or conversion, one-third of active members and one-third of affected beneficiaries would have to confirm their objection to the proposed change.

3. Effective Date for Plan Mergers or Conversions

The Proposed Framework requires that the effective date be after: (i) the date the Superintendent has consented to the merger or conversion, and (ii) the date the amendments to the SEPP (and the JSPP, if applicable) have been filed with the Superintendent. It is crucial for plan administrators to know with certainty the exact date of the proposed merger or conversion in order to provide meaningful notice to plan beneficiaries, as well as to calculate the commuted values of benefits and the amounts to be transferred from the SEPP to the JSPP.

As such, in our view, the effective date should be set by the sponsors of the SEPP and the JSPP on the basis that the determination to merger or convert is a design decision. Whether or not that conversion or merger is undertaken in accordance with legislative requirements is within the purview of the Superintendent in determining whether to provide his consent. In our view, a conversion or merger in this context is akin to a merger or asset transfer on a sale of business, where the merger or transfer is effective as of the date of the closing of the transaction.

However, the Superintendent's approval of the merger or asset transfer as of the closing date is not obtained until much later, after the legislative requirements relating to member notice, valuing of assets and liabilities and the regulatory application have been completed. Once Superintendent approval is obtained, the assets are adjusted for any investment returns or losses and payments that occurred from the closing date to the date of transfer. In this case, requiring an effective date to be determined in future that is based on the date the Superintendent consents to the merger or conversion could result in considerable changes to benefit estimates due to changes in discount rates and investment returns, resulting in significant swings in costs to be borne by one plan or the other.

In short, ACPM's view is that the effective date of a merger or conversion is a design decision to be negotiated among the parties and should be fixed in advance of the commencement of the regulatory process. We do not object to the requirement that required plan amendments to the SEPP and JSPP be filed prior to the effective date elected by the parties.

4. Special Payments for SEPP to JSPP Conversions

New paragraph 81.01(14)7 of the PBA permits regulations prescribing contributions that the SEPP employer must make to liquidate any going concern liability or solvency deficiency that exists in the SEPP at the effective date of the conversion. The proposed Regulation suggests a 10 year amortization schedule for any existing solvency deficit. ACPM is supportive of this extended amortization schedule as it will assist the SEPP employer by alleviating some of the financial pressure fully funding a solvency deficit would likely cause.

5. Asset Transfer Amount

The proposed maximum transfer amount from the SEPP to the JSPP is the greater of (i) 100% of the going concern liabilities (including indexation) for the transferring group calculated under the SEPP; and (ii) 100% of the liabilities (including indexation) being assumed by the JSPP, both calculated using the benefit allocation method.

ACPM supports the proposed calculation of the transfer on a going concern basis. The proposed 100% of liabilities calculation works relatively well where both the SEPP and the JSPP are less than 100% funded based on the benefit allocation method. However, where both the SEPP and the JSPP are over 100% funded, we have concerns with the proposed maximum transfer amount calculation. In such circumstances, the SEPP would be required to retain the surplus to distribute to plan members, notwithstanding that (a) the SEPP may have a deficit on a solvency basis as at the effective date, and (b) the employer retains a wind up deficit funding liability in respect of the JSPP (see paragraph 6 below). In addition, any surplus assets in the JSPP would effectively be "shared" with the incoming SEPP members, thereby reducing the funding buffer in the JSPP and, as a result, compromising the JSPP's sustainability.

ACPM recommends that the proposed rules be more flexible to permit the parties (SEPP employer, union and the JSPP) to negotiate a transfer amount that is appropriate in their particular circumstances. Alternatively, ACPM recommends that the maximum asset transfer amount be calculated on a cost "neutral" basis for the JSPP so that to the extent the JSPP is more than 100% funded on a going concern basis on the effective date of transfer, the JSPP's funding ratio will be maintained post-merger.

6. SEPP Employer Liability on Wind up of a JSPP after Plan Merger or Conversion

Subsections 75.1(1.1) and (1.2) of the PBA provide that where an employer has merged or converted a SEPP into a JSPP and the JSPP is subsequently wound up with a funding deficit after the merger or conversion, regulations can prescribe an amount the employer is required to pay into the JSPP for the benefit of the SEPP beneficiaries. The ACPM strongly opposes the proposed Regulation requiring the employer who sponsored the SEPP to pay into the JSPP an additional amount sufficient to fully fund the value of the SEPP benefits of the SEPP beneficiaries that had accrued up to the effective date of the merger or conversion. In light of the fact that SEPP members and beneficiaries had a mechanism to object to and thus block the merger or conversion from occurring at the outset, it is unreasonable for the employer (and its successors) to forever be liable for any wind up shortfall arising potentially decades in the future. This requirement would be unnecessarily burdensome as this contingent liability would have to be continually valued and accounted for on the employer's financial statements.

In ACPM's view, an acceptable alternative would be to require such full funding of SEPP benefits only in circumstances where a SEPP is converted to a JSPP and the JSPP winds up within 5 years after the effective date of the conversion. The objective of such a rule would be to dissuade parties to convert a SEPP to a JSPP mainly (or partly) to avoid funding an existing solvency deficit in the SEPP.

7. Expenses Incurred by Trade Unions

New subsections 80.4(21) and 81.0.1(17) of the PBA provide that where a trade union is entitled to vote on a merger or conversion on behalf of SEPP members, it is entitled to be reimbursed from the SEPP for its reasonable fees and expenses. In ACPM's view, this statutory entitlement is inappropriate and bad public policy. Unions and employers are equals across the bargaining table and, as such, each bear their own costs. In addition, the determination to merge or convert a SEPP to a JSPP is a design decision (not a fiduciary one) to be negotiated between the employer and union. Pension plans should not be required to bear any fees other than reasonable and *bonafide* administrative expenses.

However, as the PBA provides the trade union with an entitlement to “reasonable fees and expenses, of the type that are to be prescribed”, all ACPM can request at this stage is that the union’s “reasonable legal and actuarial costs” be capped, especially in circumstances where the funding ratio of the SEPP is less than 100%. If the SEPP’s funding ratio is less than 100%, the deduction of union fees and expenses will further erode the SEPPs funding status and the employer will be required to fund the shortfall through its special payments referred to paragraph 4 above. In such a case, the employer will ultimately fund the trade union’s fees and expenses. Again, this is contrary to the nature of the employer/union relationship.

Conclusion

We appreciate the opportunity to provide the ACPM’s comments on the Proposed Regulations. We would be pleased to make ourselves available to discuss or expand upon our comments and recommendations.