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Office of the Superintendent – Pension Commission
Room 1004 – 401 York Avenue
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Re: Consultation Paper – *The Pension Benefits Act* Review

We are writing in response to the above-noted Consultation Paper (Paper) released by the Department of Finance (Department) on January 10, 2018.

With almost 300 employees, working from six offices in Canada, Eckler Ltd. is the country's largest independent actuarial consulting firm. Our roots trace back to 1927, making us one of the oldest firms in the industry. We thank the Department for the opportunity to provide feedback on the Paper.

Eckler provides pension consulting and actuarial advice to a wide range of clients in both public and private sectors, unionized and non-unionized, and across all jurisdictions in Canada. Our comments reflect our own views developed based on our collective experiences and discussions with our clients.

We commend the Pension Commission (Commission) and the Department for their work on modernizing the Manitoba *Pension Benefits Act* (PBA) and Regulations, particularly in relation to the funding rules for defined benefit (DB) pension plans.

Our answers to the questions posed in the Paper are provided below.

New Plan Designs

1. Should Manitoba develop a regulatory framework for a new target benefit or shared risk pension plan design?

Yes – we believe a regulatory framework for new plan design models, including target benefit plans (TBPs) and jointly sponsored plans, should be developed to encourage employers to continue to offer registered pension plans to their members.

We believe that pension plans that pool longevity risk and investment risk will improve outcomes on average for plan members when compared to defined contribution (DC) plans. Without changing spending habits, it is almost certain in a DC plan that each and every individual will either outlive their savings or leave money behind. By pooling longevity and investment risk in a target benefit, pensions are paid for the life of each individual.

2. If so, should a target benefit or a shared risk pension plan framework be developed?

We believe that Manitoba should develop a framework for TBPs. Given that a defining characteristic of TBPs is that all of the risk associated with the pension promise is shifted from the plan sponsor to the plan members, we believe that the framework must be based on a joint governance structure with at least 50% plan member representation on the board of trustees. Other suggested aspects of the framework are as follows:

- *Administration:* TBPs should be administered by a board of trustees with at least 50% plan member representation on the board.

- *Governance:* The board of trustees should be responsible for all operations of the TBP, including the power to amend plan documents.
- *Funding:* TBPs should have a robust funding policy, with the measurement and funding of target benefits based on a going concern valuation.
- *Disclosure and Communications:* Given the ability of TBPs to adjust benefits up or down in specific circumstances, we believe that detailed and ongoing communication is required for members and other beneficiaries. We therefore support enhanced disclosure requirements for plan members and beneficiaries. Members should be entitled to receive information about the factors that can influence whether their target benefits could be increased or decreased.

3. Should the new plan design be available to both single employer and multi-employer plans, and both private sector and public sector plans?

We believe that TBPs should be available to both single employer and multi-employer pension plans (MEPPs), in both the private and the public sector.

4. Should the new plan design be restricted to unionized environments?

We believe TBPs should be available in both unionized and non-unionized environments, although additional legislative guidance may be required for non-unionized TBPs. For example, in a non-unionized environment the trustees will need to develop a democratic structure to determine governance, and legislative or regulatory guidance could be provided to assist employees.

5. Should conversion to the new plan design be permitted for future benefit accruals only?

We believe DB plans should be able to convert to TBP on both a future and a past service basis for active members much like conversion to DC is permitted. Without the ability to convert past service benefits, the impact on sustainability of converting to TBP is greatly diminished because it takes a generation for the benefits to completely turnover. Without the ability to convert any past service, we believe few TBPs will be established, as evidenced by the experience in Alberta where we understand that only one TBP has been set-up.

6. If conversion of existing benefits is permitted, should union or member consent be required?

For MUPPs and MEPPs where benefits can be reduced, we believe member or union consent should not be required for conversion. For other DB plans, we believe that any conversion should require the consent of affected plan members and retirees. Unions should be able to consent on behalf of the employees they represent. However, we are aware that there are a wide variety of consent mechanisms, and believe that employer and member groups should be able to determine which mechanism works best in their particular case - subject to the approval of the Commission.

Solvency Deficiency Funding Rules

7. Are any of the above options reasonable and practical in a Manitoba context?

When developing a new funding framework, we believe the government must ensure that it is reflective of, and responsive to, the range of plan designs and risk characteristics that comprise modern DB plans. The current DB funding rules in the PBA and Regulations were written for (and are best suited to) single employer plans sponsored by corporations or private sector businesses. However, DB plans are currently offered by a wide variety of plan sponsors, for a variety of members, and feature a range of plan designs, as shown below.

Plan sponsor classification	Plan composition	Covered members	Plan design
• Private sector • Public/Broader public sector • Not-for-profit • Industry group	• Single employer • Multi-employer	• Non-unionized • Unionized • Full-time • Part-time	• 'Traditional' DB • Hybrid • Target benefit • Jointly sponsored • Multi-employer

As there is no longer a single type of DB plan, we believe that there should no longer be a single set of DB funding rules. Instead, we believe that Manitoba should develop a range of funding rules that reflect the differing characteristics of these plans.

In order to address the funding challenges faced by all types of DB plans and plan sponsors, while providing adequate protection for plan members, we believe the new funding framework should feature rules that vary depending on a given plan's risk factors, including those relating to its investments, governance, and demographics, and the allocation of risk between employers and members. The plan sponsor's business or industry risk might also factor into the assessment. Under such a framework:

- Plans with stronger risk management practices, or lower inherent risk profiles, could be subject to more relaxed funding rules, while stricter funding requirements would apply to riskier plans.
- Plans where members are actively involved in decision-making may be subject to less stringent minimum funding rules to reflect the informed assumption of risk by plan membership.

In addition, risk-based funding may encourage plans to adopt better risk management practices to qualify for what may be considered more advantageous funding rules. This will enhance overall benefit security.

There are additional costs and potential drawbacks to implementing a risk-based DB funding framework. These include concerns relating to:

- The expense of employing and training the additional regulatory staff necessary to oversee the framework,
- The additional disclosures required by plan sponsors to ensure that the Commission, plan members and other stakeholders are adequately informed about a plan's risks,
- Concerns that an overly complex risk-assessment and risk-based funding approach may encourage plan sponsors to continue to shift away from DB plans to reduce their compliance burden,
- The plan sponsors who most desperately need relief from solvency funding are likely the ones that are at the greatest risk of insolvency.

These concerns will need to be carefully balanced against the benefits of having a funding framework that better reflects the realities facing many DB plans.

Despite the concerns noted above, we believe that the adoption of risk-based DB funding provides numerous strategic benefits:

- *Benefit Security:* Members in more at-risk plans will be subject to enhanced funding requirements, helping to safeguard their benefits. In addition, sponsors may take measures to minimize plan risks to be subject to more relaxed funding rules.
- *Affordability and Sustainability:* Flexible funding rules could increase the affordability of DB plans, and may encourage sponsors to make design changes within the DB spectrum, rather than converting or closing the plan.
- *Pension Coverage:* Flexible funding, and related sustainability improvements, should help to slow declining pension coverage, and may encourage employers to re-examine offering DB plans to their employees.

- *Transparency:* Funding requirements that are tied to the plan's risk factors lead to a clearer appreciation of the true cost of providing a DB plan.
- *Balancing Stakeholder Interests:* A risk-based system will provide sponsors with clear rules and should address concerns around cost certainty and cost level. Tying funding to risk should improve benefit security for current and former plan members, including retirees, by reducing the likelihood that a DB plan will be wound up with a significant shortfall.

Finally, it is imperative that regulatory requirements result in funding requirements that are as stable as possible. Funding rules that result in highly variable contribution requirements detract from the long-term stability of such plans and erodes member confidence in the plan’s administrators.

8. If so, which option or combination of options described above would be most effective in balancing the different interests of plan sponsors, unions, members and retirees?

We believe the best approach to DB funding is the development of a set of funding rules based on the principles outlined in our response to question 7 above. However, of the options outlined in the Paper, we believe that Option 1 is the one that will be most effective at balancing the interests of all stakeholders and promoting the stability of DB plans. Our detailed comments on Option 1 are provided in response to question 9.

9. If a regulatory framework based on option 1 is developed, which approach or combination of approaches described under option 1 should be considered?

Our comments on the various proposals outlined in Option 1 are as follows:

- *Approach A – Shorten the amortization period:* This should not be adopted in isolation, but could be adopted combined with Approach B. If Manitoba was to implement this option, it should be done over a transition period, as is currently being done in Quebec.
- *Approach B – Require a provision for adverse deviation (PfAD):* In Quebec, eliminating solvency funding entirely along with the implementation of a PfAD has provided meaningful funding relief for plan sponsors, as it has led to reduced pension contributions for most plans in the current economic environment, with the prospect of more stable funding requirements in the future. This approach is best suited to plans in stable industries with a low risk of employer bankruptcy and of plan wind-up. Adoption of this approach should be considered together with complementary reform measures to adjust commuted values based on the solvency ratio, to ensure that terminating members who choose a lump sum settlement do not harm the benefit security of other members with continuing entitlements under the plan, given that there would be no explicit funding on a solvency basis. There should be limits on PfADs so as not to result in higher funding levels. Further, for TBPs, MEPPs, and MUPPs, any prescribed PfADs should be minimized so as to not create other issues such as intergenerational equity. Additional information on the calculation and funding of any proposed PfAD is required in order to better evaluate the appropriateness of this option.
- *Approach C – Solvency trigger for enhanced funding:* The effectiveness, and desirability, of this option depends on what the percentage is – e.g., 85% or another number. Once again, additional information, including how the percentage will be set and whether it will be fixed or variable, is required in order to fully evaluate this option. Adoption of this approach should be considered together with a change to the filing frequency requirement so that annual actuarial valuations are not required while there is no solvency funding requirement. Finally, this approach should not apply to TBPs, MEPPs, and MUPPs.
- *Approach D – Consolidation of deficiencies:* This option is best provided in combination with the introduction of a PfAD. This would help ensure that, in cases where benefit security is compromised, expedited funding is required to return the level of benefit security to a specific level (e.g. 80%). We note that the federal funding rules combine the consolidation of solvency deficiencies with the use of average solvency ratios. Should Manitoba adopt this option, we believe it should be combined with longer amortization periods than are currently required.

We also note that combining the consolidation of solvency deficiencies with a longer funding period largely replicates the current (and past) temporary funding relief measures, although on a permanent basis. While this approach in isolation will provide plan sponsors with relief, it does not fundamentally change the DB funding regime, and may therefore provide an incomplete solution. It also permanently weakens the original objective of solvency funding, which is to protect members against the risk of a sudden plan wind-up with a bankrupt employer sponsor.

There are a number of plans in Manitoba where Option 3 is already in place through solvency exemption regulations where the government has deemed these sponsors to have a low risk of default. Should Option 1 be adopted, we caution against drastic changes to these plans. These plans could continue to be exempt from any solvency trigger in Approach C and could also be exempt from the additional PfADs under Approach B. We recommend that if Option 1 is adopted and applied to these plans, the application should, at a minimum, be subject to a transition period to allow these plans to adjust to any changes.

10. If the 100% solvency threshold is reduced to require partial funding, is a threshold of 85% appropriate? If not, what should the threshold be?

A key feature of the new regulatory framework should be contribution stability. We believe that the solvency funding target, and related amortization period, should align with the enhanced going concern funding rules to produce a consistent timeline for achieving the funding objectives. Manitoba should consider funding both target going concern levels and adjusted solvency levels over the same period.

It’s not clear whether 85% is the “right” number, however we do see value in having the funding rules harmonized across jurisdictions:

- Ontario has adopted solvency funding at 85%. However unilaterally reducing the solvency funding requirement in Manitoba should not be justified by the change in Ontario; Ontario has the PBGF to help protect members’ benefits, and an increase to PBGF premiums and coverage is being implemented coincidental with the reduction to solvency funding.
- Quebec has adopted no solvency funding in conjunction with the adjustment of commuted values for terminating withdrawing members based on the solvency ratio of the plan.

Again, as noted in our response to Question 9 above, this approach should not apply to TBPs, MEPPs, and MUPPs.

If Option 1 using Approach C (solvency funding required when a trigger is met) is selected by the government of Manitoba, such as funding to 85% on solvency, changes to transfer deficiency rules are required. Currently, transfer deficiencies must either be remitted or withheld for five years which coincides with the solvency amortization period. If no solvency funding is required, then paying out a transfer deficiency, be it immediately or after five years, will impair the funded status of the plan for the remaining members. As was proposed earlier in this document, adjusting commuted values based on the solvency ratio or determining a commuted value based on the going concern funded status would alleviate this issue.

11. Are there any other reforms to the funding framework that should be considered?

A. Solvency reserve accounts should not apply to plans where benefits can be reduced (i.e. TBP, MUPP, MEPP) because solvency funding should not apply to these plans. For plans other than those where solvency funding should not apply, we recommend that Manitoba permit the establishment of solvency reserve accounts (SRAs), discussed in Option 2, to allow employers to access certain contributions made to fund a deficiency where a plan subsequently shows an actuarial surplus, either through employer refunds or through priority access for contribution holidays. While introducing SRAs will not change the solvency funding rules, there is merit in permitting plan sponsors to establish such accounts. Should such accounts be introduced, we recommend that employees also be able to share in the surplus in a SRA under a contributory plan, or that separate employee SRAs be established, in cases where employees share responsibility for funding a portion of solvency deficits. We note that the SRA concept exists in Quebec, and we understand it has been relatively easy to administer thus far. Consideration may also be given to include contributions made by plan sponsors and employees towards funding going concern deficits and PfADs.

We recommend that SRAs be applied retroactively, meaning that all solvency special payments, including those made before the legislation and/or plan change to establish an SRA in a pension plan, be eligible to be held in the SRA.

B. Ontario recently proposed a change to allow a discharge of obligation for administrators that purchase annuities. We recommend that the PBA be clarified to explicitly indicate that the purchase of an annuity fully discharges any future obligation of the plan and administrator in respect of the benefit that was purchased. Some additional thought should be given to the right of surplus or a benefit reduction following an annuity buy-out if a plan wind-up occurs subsequent to the annuity buy-out. British Columbia, Quebec and Ontario all differ on this topic.

C. As noted in our response to Approach B under Question 9 above, adoption of this approach should be considered together with complementary reform measures to adjust commuted values based on the solvency ratio, to ensure that terminating members who choose a lump sum settlement do not harm the benefit security of other members with continuing entitlements under the plan, given that there would be no explicit funding on a solvency basis.

Likewise, if a transfer value is paid out to a terminating member from a multi-employer pension plan or TBP, those types of plans should be permitted to determine the amount of the transfer value based on the funded ratio determined on a going concern basis capped at 100%. The funded ratio for this purpose should exclude any prescribed PfADs. This recognizes the risk of future benefit reductions in the plan that may occur following the transfer. This will also promote uniformity among jurisdictions and within multi-jurisdictional plans.

D. As noted in our response to Approach C under Question 9 above, adoption of a solvency trigger for enhanced funding should be considered together with a change to the filing frequency requirement so that annual actuarial valuations are not required while there is no solvency funding requirement.

<u>Locking-in provisions and access to locked-in funds</u>

12. Should Manitoba develop a regulatory framework to permit locked-in funds to be accessed due to financial hardship? If so, under what conditions?

Funds transferred from pension plans to Life Income Funds (LIFs) and Locked-in Retirement Accounts (LIRAs) are required to be locked-in, as they are used to provide the account holders with retirement income. However, there are some circumstances in which individual account holders may be better served by being able to unlock some or all of the funds in their LIFs and/or LRIFs.

We have no objections to allowing unlocking for financial hardship, and suggest that the conditions for such unlocking be based on those set out in the Ontario *Pension Benefits Act* and regulations. Ontario's framework:

- Permits withdrawals based on four categories of financial hardship (low expected income, payment of first and last months' rent, payment of rent or mortgage arrears, and payment of medical expenses);
- Uses standardized forms developed by the Financial Services Commission of Ontario; and
- Places the responsibility for approving/denying withdrawal applications, in accordance with legislative requirements, on the financial institution holding the locked-in funds, rather than on the regulator.

13. Should other reforms to the locking-in provisions in the PBA be considered?

With respect to the current regulations for unlocking 50% from a pension plan or a life income fund, place the responsibility for approval of unlocking applications on the administrator or financial institution holding the locked-in funds, rather than on the regulator.

Compulsory pension plan membership

14. Should Manitoba continue to require compulsory pension plan membership as a condition of employment where there is a pension plan in effect?

We see no reason this should change. We believe this provision increases the number of employees covered by registered pension plans.

15. Should members be permitted to opt out of plan membership?

We do not believe members should be able to opt out of compulsory plan membership.

16. Should members be able to set their contribution rate to 0% if a specified period has passed since they started contributing to the plan (e.g. 12 months)?

We do not believe members should be able to set their contribution rate to 0%. Presumably this would apply only to DC plans. However, not providing a similar rule for DB members could be considered unfair to those members, and allowing members the ability to choose not to contribute to a DB plan should not be permitted. On that basis it should not be allowed for DC plans.

Division of pensions on relationship breakdown

17. Should the current framework requiring a mandatory 50/50 division of the pension earned during the period of the relationship be maintained?

We do not believe that Manitoba should continue to mandate 50/50 division. There is no demonstrated need for such a requirement, and it is inconsistent with all other Canadian jurisdictions. Along with a person's home, a pension can represent a very large proportion of the assets to be divided in the event of a relationship breakdown and the division rules would be improved by providing additional flexibility to divide pension assets. Accordingly, we believe that this requirement should be replaced with the legislative provision discussed in our response to question 18 below.

18. Should the current framework be amended to permit parties to determine the portion of the pension to be divided, subject to the spouse or common-law partner receiving no more than 50% of the pension earned during the period of the relationship?

Yes – we believe that the PBA should be amended to provide that the pension benefit accrued during the relationship be divided based on the parties' settlement instrument (court order, agreement, arbitration award), with a maximum of 50% of the value of the pension earned during the relationship being assigned to the non-member spouse.

Clarification/legislative gaps

19. For plans not already designated as a multi-unit pension plan (MUPP), is it reasonable in a Manitoba context to replace MUPPs with multi-employer pension plans and specified multi-employer pension plans, consistent with the provisions in other jurisdictions and the Income Tax Act (Canada)?

Careful consideration should be given to MUPPs, and any change to allow new plan designs such as TBPs and MEPPs, and the funding rules associated with those plans, ensure that existing MUPPs are not adversely impacted by any changes creating additional administrative, legal or financial burdens for existing MUPPs.

20. Should the provisions setting out when an individual ceases to be an active member of a DB Plan be amended to provide that a member can choose to suspend membership and contributions at normal retirement age (normally age 65) while remaining employed, and upon subsequent commencement of a pension, receive the actuarially increased value of the pension accrued to age 65?

We believe that this should be permitted but not required, i.e. it would be an option of the plan sponsor to include such a provision. This should have also been the case when the current subsection 21(9.1) was added to the PBA in 2010 and it should be corrected.

In our experience, for many members retiring after normal retirement date the actuarial increase exceeds the formula pension on the postponed retirement date. It stands to reason that for some plans, members could be permitted to cease contributions after normal retirement date and receive no further pension accruals. However, making this change would have a financial cost on the plan as it would forgo those members' contributions after normal retirement age. In many cases, pension plans are negotiated between the employer and unions, and we believe that any change that has a financial impact should be negotiated through collective bargaining where unions are involved.

The PBA currently provides that the normal retirement age for any plan must be no later than the first day of the month following the month in which unreduced benefits are payable to a member under the Canada Pension Plan, currently age 65. However, in the University sector many faculty members start and end their careers later than the average of the general workforce in Canada. The typical, or "normal", retirement age for faculty is later than age 65. It is also becoming more commonplace for employees to continue working past age 65. The Canada Pension Plan has been amended to allow for continued contributions and pension increases after age 65.

For those reasons we believe plans should have the ability to not provide an actuarial increase and the normal retirement age should be permitted to be later than age 65 with actuarial increases only being provided after the normal retirement age (rather than age 65).

21. Should the provision setting out entitlement to ancillary benefits be amended to clarify when an ancillary benefit is vested and must be included in the calculation of commuted values?

Yes.

22. Should the pension committee requirements be amended to clarify that if there is no inactive member in the plan, or no inactive member willing to be on a pension committee, the inactive member position can remain vacant?

Yes.

Conclusion

We thank you again for the opportunity to provide our comments on the Proposal. Should you have any questions on the topics discussed above, or wish to discuss any other aspect of the Proposal, please feel free to contact Andrew Kulyk at 204-988-1572, or by email at akulyk@eckler.ca.

Regards,

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