OCUFA SUBMISSIONS

in response to

PROPOSED REGULATIONS TO FACILITATE THE MERGER OF BROADER PUBLIC SECTOR SINGLE EMPLOYER PENSION PLANS WITH EXISTING JOINTLY SPONSORED PENSION PLANS OR CONVERSION TO NEW JOINTLY SPONSORED PENSION PLANS

February 27, 2015

I. INTRODUCTION

These submissions concern Ontario's proposed framework (the "Proposals") for asset and liability transfers between single employer pension plans and jointly sponsored pension plans in Ontario's broader public sector.

The Proposals are further to Schedule 26 of Ontario's 2014 Budget Bill which set out the statutory framework for transfers of pension liabilities and corresponding assets between single-employer sponsored pension plans ("SEPPs") and jointly sponsored pension plans ("JSPPs"). Those transfers are permitted within a plan, by converting that plan from a SEPP to a JSPP, or by way of merging or amalgamating a SEPP with a JSPP.

II. ISSUES RAISED BY THE PROPOSALS

There are a number of significant issues raised by the Proposals:

1. Consent, and relationship between collective bargaining and a SEPP to JSPP conversion, and, relatedly, the definition of a 'trade union' for purposes of the consent mechanism;

2. The mechanics of transferring assets and liabilities from a SEPP to a "new" JSPP – a JSPP that, at the time of the initial transfer(s), may have no participating employers, no members and no assets;

3. The contents of notices to members, former members and retired members, especially in relation to any residual surpluses in the SEPP and any proposed distribution of those surpluses;

4. The nature of the proposed commuted value ("CV") protections on a conversion – whether they are a form of protection for each individual's accrued benefits or for the aggregate value of all members' accrued benefits, whether they should exempt the value of grow-in benefits, how they treat members of hybrid and defined contribution plans and whether the CV protections have any funding implications, either on the conversion or subsequently;

5. The residual funding obligations regarding a SEPP after an asset and liability transfer to a JSPP, and whether an employer's post-conversion funding obligations relate to the SEPP or the JSPP or both;

6. The rationale for restrictions on the maximum amount that may be transferred from a SEPP to a JSPP at conversion;

7. The treatment of surpluses remaining in a SEPP after conversion, especially if the SEPP has no active, deferred or retired members post-conversion;

8. The effective date of a conversion, and whether the mechanics for fixing the effective date are compatible with the timeline for an asset transfer;

9. The expenses of the trade union in relation to the conversion.

A. Consent and Collective Bargaining

The *Pension Benefits Act* ("PBA") has been amended to provide a framework for pension asset and liability transfers in the BPS. Among other things, section 80.4(6) of the amended PBA requires that "…the members, former members, retired members and other persons entitled to benefits under the single employer pension plan **consent** to the proposed conversion and transfer of assets, **or are deemed in accordance with the regulations** to have consented to the conversion and transfer" (emphasis added).

We write specifically about the relationship between these consent provisions and the rights of collective bargaining agents. It is generally understood, and has been specifically understood in the University sector, that the consent provision is not intended to and may not override the collective bargaining agent's ability to determine, through collective bargaining and a collective agreement, the terms and conditions (including the pension terms and conditions) of its members' employment. However, the consent provisions of the Proposals, read with section 80.4(6) and (19) of the amended PBA – which require consent and then deem section 80.4 to prevail over any collective agreement – clearly override a collective bargaining agent's ability to exercise its collective bargaining mandate. These provisions are plainly unacceptable in their current form, and must be changed.

The Proposals specify two consent requirements, one for active members and the other for all other plan participants:

- 2/3 of active members would have to consent to the transfer; and
- no more than 1/3 of former members, retired members and other beneficiaries, considered together as a group, could object to the transfer.

Active member consent may be provided by a trade union that represents the active members.

If the twin consent requirements are met, then all other members, former members, retired members and other beneficiaries would be deemed, under the Proposals, to consent to the transfer.

These consent provisions place any bargaining agent with fewer than 1/3 of a SEPP's active members in the position where their collective bargaining rights, and the bargained terms and conditions of their members' employments, may be overridden by other bargaining agents and persons outside the bargaining unit. Most University pension plans have members who belong to no trade union (many of whom are management employees), and most plans are multi-union plans; in this environment, it is appropriate that a third condition for consent be prescribed, namely that the consent of each bargaining agent with members in the plan be obtained in order for the statutory consent requirements to be met. This is the only way that the laws governing collective bargaining and the provisions of the amended PBA can be reconciled. It is also the only way that a respectful and effective transition process may be designed.

Accordingly, OCUFA recommends that the consent provisions of the proposed Regulations contain an express requirement that the consent of each collective bargaining agent with members in the SEPP be obtained in order that the statutory consent requirements of section 80.4(6) of the amended PBA be met.

Relatedly, the definition of 'trade union' must be carefully considered in the University sector because some faculty associations may not be trade unions for the purposes of the Labour Relations Act, yet may collectively bargain terms and conditions of employment, including compensation terms, on behalf of their members. These faculty associations should be deemed to be trade unions for purposes of the consent provisions.

B. Transfers from a SEPP to a new JSPP

The amended PBA and the Proposals both assume that a conversion from a SEPP to a JSPP is to an existing JSPP rather than a new JSPP. However, in the University sector, the COU and OCUFA together with other employee groups are in the process of designing a new multi-employer or sectoral JSPP that, in principle, could receive assets and liabilities from University sector SEPPs. There is a general recognition that this leaves a gap in the Proposals and that it is desirable to close that gap so that transfers from a SEPP to a 'new' JSPP are permissible.

The 'gap' under the amended PBA and the Proposals arises from the fact that the recipient plan must be a JSPP, which is a defined type of plan under the PBA that must be registered under the PBA. Until a plan is registered, it cannot be a JSPP for purposes of the PBA. Further, the amended PBA requires that the 'sponsors' of the JSPP must enter into an agreement for the asset/liability transfer with the SEPP employer – so the JSPP must not only be registered under the PBA with the Financial Services Commission of Ontario ("FSCO"), but must also have 'sponsors' prepared to act as such. In sum, the recipient JSPP in a conversion transaction must be registered with FSCO under the PBA and must be in a position to receive assets and grant past service credits as of the effective date of the transfer, and to accept contributions and grant future service credit to the transferred members from and after the effective date.

This is a gap that should be addressed as soon as possible. Although a technical issue, it is a complicated technical issue whose solution may have ramifications for other aspects of the Regulations or for the design of the new University JSPP itself.

In our submission, there are two aspects to the gap that may be addressed in two different ways. First, it may be worthwhile to consider, with FSCO, whether FSCO would register a University JSPP before the JSPP has any members, participating employers or assets, or whether regulatory provisions would be necessary for this to happen. Second, it will be necessary to ensure that the new JSPP is able to fulfill its responsibilities in negotiating an asset transfer arrangement with the SEPP. If the JSPP has no resources, it will not be in a position to effectively determine the terms of an appropriate asset transfer arrangement.

In the same vein, it is apparent that a new University sector JSPP can only succeed if it is exempt from solvency funding requirements. The new Plan will be voluntary and

participation in it will require the consent of the employer and the members; if the new Plan must be funded on a solvency basis, it will not attract the interest of stakeholders. In this respect, we believe that the employee stakeholders, and the employers, as represented by the COU, are in complete agreement. Accordingly, a Regulatory provision exempting the new Plan from solvency funding requirements would be welcome, at the earliest opportunity.

Accordingly, OCUFA recommends that a joint approach be made to FSCO to determine whether it would register a new University JSPP without any members, participating employers or assets, or whether regulatory amendments would be necessary in order that the new JSPP obtain registration with FSCO under the PBA. Relatedly, consideration must be given to the new JSPP's capacity to fulfill its statutory mandate to negotiate transfer agreements with University SEPPs. The Regulations should also clearly exempt the new University JSPP from solvency funding requirements.

C. Notices to Members, Former Members, Retired Members and Trade Unions in Regard to Residual Surpluses in a SEPP

The Proposals contain additional information elements to be included in notices to members, former members, retired members and trade unions in regard to a proposed conversion from a SEPP to a JSPP.

In the event of a residual surplus in the SEPP, notices should also advise members, former members and retired members, as well as their trade unions, of the amount of any residual surplus and of the proposed distribution of the residual surplus. In practical terms, the distribution of any residual surpluses will be integral to the conversion process, and should be a regulated aspect of the conversion process.

Accordingly, OCUFA recommends that the notices to members, former members, retired members and trade unions should also advise them of the amount of any residual surplus and of the proposed distribution of the residual surplus.

D. Treatment of Commuted Values ("CVs")

The amended PBA requires that, in the event of a conversion from a SEPP to a JSPP, the commuted values ("CVs") of the benefits provided under the JSPP as of the effective date of the transfer be not less than the CVs under the SEPP (see section 80.4(13)(7)).

There remains an ambiguity in the amended PBA, which is not clarified in the Proposals, as to whether this protection is an individual protection (i.e. each individual's CV may not be reduced, as of the effective date) or whether this protection operates on a collective basis (i.e. the aggregate of the CVs of all members may not be reduced as of the effective date). This ambiguity may have plan design implications, and so should be addressed as soon as possible.

The Proposals specify that the CVs in the SEPP are to be calculated without regard to grow-in benefits – this means that the SEPP CV values as determined for purposes of

the conversion and the CV protections under the PBA amendments, will be less than they actually are under the SEPP. The rationale for this is that JSPPs are entitled to and have generally opted out of the grow-in rules. But the Proposals would exclude grow-ins from the SEPP CV calculations regardless of whether the JSPP has opted out of grow-ins. Moreover, this aspect of the Proposals implies a reduction in the CVs of transferring members – contrary to the general policy premise underlying conversions that the transaction should be neutral at worst for all members as at the effective date.

Similarly, the CV protection proposals do not work well with the type of contingent indexation benefits prevalent in the University sector. In many cases, excess earning indexation provisions will have no CV at all. This means that they could simply be eliminated without violating the CV protections, and we do not believe that this is the intended result. These provisions would have to be replicated to be protected. This concern, though clear enough in the case of contingent indexation benefits, also applies to other benefits with a contingent aspect.

The CVs of hybrid plan members and defined contribution plan members also require consideration. How will they be treated on a transfer? The Proposals are silent with respect to minimum standards for CV protections for these SEPP members on a conversion to a JSPP. The COU has raised similar concerns, underlying the stakeholder interest in clarity regarding the treatment of members currently in DC and hybrid plans. In our submission, the Regulations should ensure that prospective University JSPP members who belong to hybrid or defined contribution plans will view the new JSPP as providing the same level of benefit protection as they currently enjoy under the relevant University SEPP.

The Proposals treat the CV guarantee for transferring members as a form of benefit protection that is in lieu of a regulatory minimum transfer amount. However, this protection is only on the benefit side; there seems to be no corresponding requirement that the JSPP have sufficient assets on the effective date to pay all the CVs for all members who transfer to the JSPP. Indeed, as set out below, it is impossible under current circumstances, for an asset transfer to comply with the Proposals and yet be sufficient to cover the CVs of the transferring members, former members and retired members. This is because the Proposals prescribe maximum transfer amounts that are determined on a going concern and that will necessarily be lower than CV values at this time.

Accordingly, OCUFA recommends that the proposed Regulations:

- **clarify that the CV protection is an individual protection that applies as of the effective date and requires that a transferring member's CV under the JSPP be not less than the transferring member's CV under the SEPP;**

- **require that the CVs determined under the SEPPs include the commuted value of the member's grow-in benefit;**

- **require replication of all benefits with a contingent aspect, including contingent indexation benefits;**

- **expressly address the treatment of the CVs of members of hybrid SEPPs in a manner than ensures that their CVs in the JSPP are not less than the value of their CVs under the hybrid SEPPs;**

- **leave the asset transfer amount in a conversion from a SEPP to a JSPP for negotiation between the SEPP employer and the sponsors of the JSPP and not contain any provisions limiting the amount of an asset transfer in a conversion.**

E. Funding of SEPP after JSPP Transfer

The Proposals contemplate residual going concern unfunded liabilities and solvency deficiencies in the SEPP, after the transfer to the JSPP. They permit the SEPP's residual solvency deficiency to be re-amortized over 10 years. The Proposals are silent about the going concern unfunded liabilities – presumably, any going concern amortization schedules at the time of conversion remain in place.

These aspects of the Proposals require some clarification – if all liabilities have been transferred from the SEPP to the JSPP, how can the SEPP have a solvency or a going concern deficiency? If the SEPP has no members, and the special payments create a surplus, how is that eventual surplus to be distributed?

It would appear that these provisions would apply only when the JSPP is not solvency exempt – where the JSPP is solvency exempt, the Proposals specify that any pre-existing solvency or going concern payments would be cancelled (page 14, section 8 of the Proposals). This approach requires clarification – why are payments to the SEPP continued, rather than directed to the JSPP; why is the Proposal silent in regard to going concern payments where the JSPP is not solvency exempt; how are surpluses that may arise as a result of special payments to be addressed, if the SEPP has no members?

Accordingly, OCUFA recommends that the proposed Regulations clarify the residual funding obligations in regard to a SEPP after conversion.

F. Transfer Amount – SEPP to JSPP

Under the Proposals, the amount to be transferred from the SEPP to the JSPP is to be negotiated. The Proposals stipulate no minimum amount to be transferred. Accordingly, the negotiation process is important for a SEPP to JSPP conversion and transfer. This implies that the JSPP must be properly staffed and advised for the conversion/transfer negotiations.

If the SEPP doesn't have enough assets to satisfy the negotiated transfer amount, the Proposals would allow the SEPP employer to make up the difference in equal monthly instalments over 15 years (Pages 13/14, section 9 of the Proposals). This is the standard amortization schedule for a going concern unfunded liability.

Although there is no regulated minimum transfer amount, the Proposals do specify a maximum transfer amount, and would prohibit SEPP to JSPP asset transfers in excess of this regulated amount. The maximum transfer amount is calculated on a going concern basis (apparently, even where the JSPP is not solvency exempt), and is equal to the greater of the going concern liabilities associated with the transferred service under the SEPP and the going concern liabilities associated with the same service under the JSPP. In each case, the going concern liabilities must include "any indexation under the SEPP".

A guiding principle under the Proposals is that the JSPP should not be worse off, i.e. its funded ratio should not decline, as a result of the asset transfer. This is unobjectionable, and reflects the JSPP's fiduciary obligations to existing members to protect the JSPP's funded position in any negotiation over transfer amounts.

The proposal for a maximum transfer amount, however, is more problematic. The Proposals suggest that a regulated maximum amount is appropriate for two reasons – (i) to preclude a funding buffer in the JSPP and (ii) to prevent the parties from avoiding surplus issues under the SEPP. The Proposals also note that any transfer 'should avoid transferring excess assets', since this would benefit all JSPP members and not only the transferred members.

However, a regulatory maximum asset transfer amount gives rise to several questions:

1. Why do the Regulations need to specify a maximum transfer amount at all? The principled approach to asset transfers in this context is that arms-length negotiations between sophisticated parties may be relied upon to generate a mutually agreeable asset transfer amount. On the other hand, the arms-length negotiation anticipated by the Proposals seems artificially constrained by a regulated maximum transfer amount.

2. The rationales advanced in the Proposals for the regulated maximum - to preclude a funding buffer in the JSPP and to prevent the parties from avoiding surplus issues under the SEPP - aren't critical. Funding buffers are generally positive for pension plans and are increasingly favoured by minimum standards funding rules. In any event, there is nothing to prevent a JSPP from creating funding buffers simply by adjusting going concern assumptions. Surplus withdrawals are generally a negative insofar as they deplete the closed pension funding system.

3. Why is the maximum amount defined in going concern terms, especially in regard to JSPPs that are not solvency exempt?

4. What is meant by "any indexation under the SEPP must be included in the calculation of the transfer amount"? How does this apply to funded and unfunded target indexation formulae, excess return based indexation formulae or ad hoc indexation provisions?

5. CAAT raises the point that, if the recipient JSPP is in surplus at the effective date, the consequence of the maximum transfer amount is that the JSPP must

dilute its funding level because it cannot accept any surplus from a SEPP. This contravenes the basic principle that the JSPP should not be adversely affected by the transfer, and could put the recipient JSPP in a difficult position if it is in surplus when negotiating a SEPP to JSPP conversion/transfer.

Accordingly, OCUFA recommends that the proposed Regulations contain no regulated maximum transfer amount in a SEPP to JSPP conversion and asset transfer. Rather, the amount transferred into the JSPP should be determined through negotiations between employer and employee groups and should not be constrained by regulatory limits. We note that the COU adopts the same position, and also opposes regulatory limits on asset transfer amounts.

G. Surpluses Remaining in SEPPs After Transfers

The Proposals specify that any surpluses remaining in the SEPP after an asset transfer would be distributed in accordance with the PBA.

The PBA contains a number of provisions regulating how surpluses in a pension plan may be distributed. The starting point for the PBA surplus regulatory provisions is section 77.11(1), which provides that the foundational documents of a pension plan "govern the entitlement of the employer and other persons to payment of surplus under the pension plan, except as otherwise provided under this Act and subject to the restrictions on payment set out in sections 78 and 79."

Section 77.11(2) provides that a pension plan which is silent on the treatment of surplus when the plan is ongoing "shall be construed to prohibit the withdrawal of surplus money accrued after December 31, 1986". Pursuant to section 77.11(3), if a pension plan is wound up which does not provide for the treatment of surplus, the surplus that has accrued after December 31, 1986 must be "distributed proportionately...among members, former members, retired members and other persons entitled to payments under the pension plan on the date of the wind up".

The PBA thus recognizes two basic approaches to the disposition of surpluses in a registered pension plan: a) surplus may be distributed in accordance with the documents that "create and govern" a pension plan where they provide for its treatment; or b) surplus can be distributed on wind up amongst the members, former members, retired members and other beneficiaries.

In addition to these two plan document-based approaches to the distribution of surplus, and regardless of which surplus treatment would otherwise apply, section 77.11(7) allows for an agreement about the treatment of surplus -- both in an ongoing plan and on wind up -- between the employer, two-thirds of the members, and an "appropriate" number of former members, retired members and other persons entitled to payments from the plan. Section 77.11(8) establishes the primacy of such an agreement, mandating that it "prevails over" all foundational documents of a pension plan, over any deeming under subsections (2) and (3), and over "any trust that may exist in favour of any person".

The PBA's surplus regime raises difficult questions in relation to its application to SEPP to JSPP conversions and asset transfers. Once the members of a University SEPP transfer their pension entitlements - and all associated assets and liabilities - to the JSPP, those members (the "JSPP Members") will have no status under the PBA in relation to their prior membership in the SEPP. They will not be "members", "former members", "retired members" or "other persons entitled to payments under the pension plan" as those terms are defined in the PBA (see section 1 and 1.1 of the PBA). Those people who join the new JSPP and whose past service benefits are transferred to the JSPP would not be eligible to participate in a surplus sharing agreement in relation to their former SEPP, nor would they be entitled to share in the surplus under the statutory provisions described above, even though the University sector SEPPs are typically contributory and any surpluses remaining in them after a conversion and asset transfer would be at least partly attributable to member contributions and/or other historic elements of the collective bargaining process.

Any residual surpluses in the SEPP after a SEPP to JSPP conversion and asset transfer must recognize the rights and entitlements of those persons who were members, former members and retired members of the SEPP immediately prior to the conversion. Any approach that fails to recognize their status and entitlements is unfair and reflects an inappropriate employer bias. Moreover, in practical terms, it is highly unlikely that any group of members, former members or retired members would consent to any conversion or asset transfer if a resulting residual surplus in a SEPP were not dealt with fairly.

By the same token, a distribution of residual surplus should take place within a reasonable prescribed period of the conversion. Otherwise, as members, former members and retired members, and their spouses and beneficiaries, die, their entitlements to a surplus share will, in practical terms, disappear.

Accordingly, OCUFA recommends that the proposed Regulations expressly treat persons who were members, former members and retired members in a SEPP immediately prior to a conversion and asset transfer to a JSPP as continuing members, former members and retired members of the SEPP, after conversion, for purposes of any surplus distribution. Moreover, residual surpluses should be distributed within a prescribed period of the conversion.

H. Effective Date

CAAT raises a technical issue in regard to the Proposals that we believe applies as well to the ‘new’ JSPP currently being developed. CAAT’s concern is that the ‘effective date’ under the Proposals must be a day following the Superintendent’s approval of the asset transfer. Unfortunately, there is no time limit on the Superintendent’s approval process, so the effective date may be long after the negotiations over the transfer agreement have concluded. By that time, circumstances, including interest rates and investment returns, may have changed significantly. CAAT urges an earlier effective date – after the consent process, in the case of mergers.

We agree with CAAT's concerns and endorse its recommendations in this regard. The COU has also expressed concerns regarding the timing of the Superintendent's approval, with which we agree.

I. Expenses of Trade Union

Section 80.4(21) of the amended PBA provides that a trade union entitled to vote on a SEPP to JSPP conversion and asset transfer may be reimbursed from the pension fund "…its reasonable fees and expenses, of the type that are prescribed, relating to the vote."

As a practical matter, trade unions typically cannot afford the costs entailed in the due diligence appropriate for this type of conversion. Accordingly, reimbursement of their expenses is a necessary precondition for this process. It is also an appropriate condition, since the process created by section 80.4 was not in any fair contemplation of a trade union's duties and responsibilities in the normal course.

The costs of a trade union entitled to vote in the section 80.4 process are not easy to foresee. Clearly, the trade union will have to evaluate, with actuarial, legal and internal labour relations or project management expertise, any conversion and asset transfer proposal that may be proposed by a SEPP employer or negotiated between the SEPP employer and the JSPP. The trade union may then recommend changes to the conversion and asset transfer proposal, and may engage in negotiations to vary the proposed terms of the conversion and asset transfer. It will conduct an internal communication and decision-making process, which may be quite extensive, so that affected members are well informed about the proposal. In practical terms, unless the trade union performs all of these functions, it is unlikely to be in a position to consent to any conversion and asset transfer. All expenses that are out of the trade union's normal course dues funded activities, and are in relation to a SEPP to JSPP asset transfer proposal, should be reimbursable.

Accordingly, OCUFA recommends that the proposed Regulations provide for a trade union's reimbursement for all fees and expenses related to its due diligence concerning any proposed asset transfer from a SEPP to a JSPP, including fees and expenses incurred for actuarial, legal, labour relations, project management or other relevant assistance, should be reimbursed to the trade union.