Public Service Alliance of Canada
Alliance de la Fonction publique du Canada

SUBMISSION BY THE PUBLIC SERVICE ALLIANCE OF CANADA

TO THE PENSION COMMISSION OF MANITOBA

REGARDING ITS CONSULTATION PAPER "THE PENSION BENEFITS ACT REVIEW"

FEBRUARY 2018

POSITION OF THE PUBLIC SERVICE ALLIANCE OF CANADA

PSAC represents 180,000 members, the vast majority in the federal public sector. In Manitoba, PSAC represents approximately 1,150 employees in eight bargaining units, covered by provincial pension legislation. Of these, 515 are employed at Deer Lodge Centre and participate in the Manitoba Health Employees Pension Plan (HEPP). A total of 425 PSAC members are employed at Brandon University and the University of Manitoba. Due to the nature of their employment, the majority of these members are not permitted to participate in their respective pension plans.

EXECUTIVE SUMMARY

Reforms to the Manitoba *Pension Benefits Act* (PBA) are not needed to convert good pensions into pensions that provide unreliable benefits.

The key objective of any pension system is to provide decent, secure and predictable pensions. Any conversion of defined benefit to target benefit plans will not achieve this objective. To the contrary, target plans will shift financial risk from employers to employees and pensioners, increase pension uncertainty and reduce pension benefits.

Canadians require decent pensions upon which they can rely — pensions that are secure and predictable, and that allow them to plan their retirements accordingly. Not knowing how much a pension will be next week or next year undermines the retiree's security in retirement, compromises the retiree's quality of life and weakens the retiree's ability to participate in their community and support their local economy.

Existing benefits earned and paid for by members, and backed by their employer's promise to pay any deficiency must not be stripped of that employer promise, through, for example, a so-called voluntary consent process that provides ample opportunity for employers to apply undue pressure on employees and retirees. This will mean that employers will be allowed to break the pension promises they have made to their employees and pensioners, who will suffer pension uncertainty and benefit reductions as a result.

Target plans will be complex and expensive to administer, and will offer benefit security based on models of a future that is 20 years away; no models are capable of predicting the future to a 90% level of certainty, and any promises based on such models are simply misleading and corrosive of Canada's pension system.

Target benefit pension plans are not the appropriate solution and do not provide the platform employees need for their retirements; target plans will become part of a growing retirement income problem in Canada not its solution.

Predictable and secure pensions are not the problem that requires addressing today. The real pension problem is that two thirds of Canadians have no workplace pension at all. They rely on the Canada Pension Plan and a hodgepodge of high-fee, finance industry-friendly private retirement savings plans that are inadequate to the task of real retirement savings.

The challenges facing private and broader public sector pension plans — including funding challenges — can be met and addressed in a variety of ways, including targeted solvency relief, joint governance platforms, and others. Each of these should be part of a balanced package of reforms.

New Plan Designs

Target benefit pension plans and other shared risk pension plans reframe the nature of the pension promise that employers make to their employees and retirees, and this will have profound impacts on those employees and their families.

The basic purpose of a pension plan is to provide decent retirement incomes that are secure and predictable. Decent, secure and predictable pensions give their recipients "pension confidence". Pension confidence means that people, while they work, can spend their earnings, knowing that their retirement days are secure. As important, pension confidence also means that retirees can spend each pension cheque, knowing with confidence that their income stream is not in doubt. Pension confidence underpins the economies of many small communities with significant pensioner populations and the small businesses that serve them.[1]

- **Not enough people have access to decent pension plans**

The real problem in the pension sector is the number of people who do not participate in decent pension plans. In some cases, employees without pension plans earn incomes that allow them to save for retirement, but the savings mechanisms available to them from financial institutions are typically expensive and inefficient in comparison to large scale pension plans. In other cases, a decent pension plan is the crucial bridge that could allow modest income earners to save enough for a decent retirement. In all cases, the lack of pension coverage hurts the province.

Looking forward, for example, Professor Michael Wolfson projects that half of Canada's middle income earners will experience a significant decline in their standard of living standards after retirement. In his paper, "Projecting the Adequacy of Canadians' Retirement Incomes[2], published by the Institute for Research on Public Policy in April 2011, Professor Wolfson concluded that "…roughly half of Canadians born before 1970 who had mid-level earnings in their pre-retirement years will face declines of at least 25 percent in their living standards (i.e., consumption possibilities) post-retirement." These findings have been confirmed in other studies of income replacement prospects for Canadians[i]. This failure is largely owing to the inadequacy of pension coverage in Canada. This is the real problem that presses for a solution.

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[1] See, for example, the positive economic effects of defined benefit plans set out in Boston Consulting Group's report, *Defined Benefit Plans: Strengthening the Canadian Economy*, October 22, 2013, available online at: www.otpp.com/news/article/-/article/701993.

[2] See also LaRochelle-Coté, S., J. Myles, and G. Picot, 2008. Income Security and Stability during Retirement in Canada. Analytical Studies Branch Research Paper Series no. 306, Ottawa: Statistics Canada.

Target benefit plans are not new in Canada — they have existed in the multi-employer pension plan space for some time. Industries that have adopted the multi-employer model include construction and transportation — typically industries in which there is a higher risk of employer insolvency or exit. Experience with multi-employer pension plans suggests that some of the key governance features — reflected in legislation and regulations of multi-employer plans — are essential to their successful management.

The most important feature is the relationship to collective bargaining. Multi-employer target benefit plans require at a minimum there be some form of joint governance of the plan, so that the risks the members are exposed to can be managed by their representatives. In the public and broader public sector joint governance has often been achieved through the jointly-sponsored, jointly-governed plans that provide secure and predictable defined benefits.

A funding policy is required to state the benefit formula and subsequent changes to it, as well as contribution rate changes and deficit amortization and surplus use policies. Each of these may be subject to regulation. It may be that the regulations themselves will be overly prescriptive with these key features — or not. For example, will funding policies prohibit the application of surplus to employer contributions? In a target benefit plan, in which members and retirees bear all the relevant risks, they should also own all the relevant rewards and should be a condition of a funding policy.

- **New pension plans will not be created**

Target benefit plans do not address the fundamental problem of pension coverage. Employers will not establish new target benefit plans where no plan currently exists, and they will not convert existing defined contribution plans to target plans. Introducing target benefit plans will allow employers to convert good defined benefit plans that provide decent, secure and predictable benefits, into the much less secure form of target benefits. **No such conversions should be permitted; good pension plans must be preserved and expanded, not downgraded.**

- **Earned pension promises will be broken**

Any suggestion that benefits already earned and paid for by a member in a defined benefit plan—including by retirees—may be cut is outrageous. With target benefit plans, accrued defined benefits may be converted to target benefits, and those target benefits may be reduced. The very benefits towards which members have worked and made contributions, and that have been guaranteed by their employers, may be converted to target benefits guaranteed by nobody.

Pensions provide life income benefits that people depend upon when they can no longer work. But target benefit pension plans do not provide this certainty. No one would deposit money in a bank account if their account balance could be reduced at any time and in any amount. No one would agree to pay premiums for a life or other insurance policy if the amount of coverage could be reduced at any time or in any amount. And it would be of little help for the bank or insurance company to say, based on their models, that there is a 90% chance the bank account or insurance policy would retain its value.

The models upon which such projections are based are not good enough to provide any real level of comfort at all. After all, much more sophisticated financial models failed in the 2008-09 financial crisis. People want and deserve certainty in their financial products, and nowhere more so than in their pension plans. It is the government's role to regulate financial products, including pensions, so that financial promises are kept.

In PSAC's view, promises made should and must be kept. The most basic purpose of pension regulation is to ensure that people can rely on their employers' pension promises, and that those promises are kept.

- **Voluntary consent provisions are a sham**

Employers stand to gain much from converting to target benefit plans. As a result, they are motivated to use every short-term incentive and every pressure tactic they have to compel and persuade employees and retirees to surrender their protected defined benefits for unprotected target benefits. Employers can threaten job losses and cost-cutting or offer short-term incentives such as lump sum cash payments or improvements in paid leaves or welfare benefits that are appealing at the time of offer.

The protection of guaranteed vested pension benefits has been the core objective of pension regulation in Canada. Employers have made defined benefit commitments with their eyes open. Employees have worked and contributed to earn those benefits. Vested pension benefits, promised and earned, are delivered. To permit those vested benefits to be undone, even on the basis of a so-called consent process, is unconscionable.

- **The New Brunswick example is not a model**

New Brunswick illustrates the perils of the target benefit regime. The provincial government introduced the "shared risk plan" — a form of target benefit plan, claiming buy-in from trade unions and retirees in the process.

In fact, as more details emerged about these plans, the true risk and nature of them became apparent, and litigation over these plans has ensued. Furthermore, these risks and nature were obscured, even by the name of these plans, as "shared risk". As the Government of New Brunswick admitted to the province's Auditor General, there is nothing "shared" about the risks under the New Brunswick target plan model – the risks (investment, mortality and ultimately, of benefit reductions) are overwhelmingly on the members and retirees in those plans, with employers bearing no risk in regard to them at all.

The New Brunswick example also includes plainly misleading assertions about the security of retirement income benefits. Some of these assertions are based on future modelling, which has the appearance — but not the reality — of scientific accuracy, expressed through complicated and overly-deterministic regulations. The modelling behind those regulations has not yet been successfully confirmed by independent third parties, and yet an entire public pension system was converted on the basis of it. As New Brunswick's promises fail, confidence in its system will falter and stakeholders will become justifiably angry.

As we noted above — the lack of clarity and the false confidence placed in projection models (which are very sensitive to small changes in assumptions and not well understood) creates an environment for uncertainty and misleading information about pension plans, an already complex area for members and employers alike.

AN ALTERNATIVE: **The most successful pension model in Canada — jointly sponsored defined benefit plans**

Within the sphere of workplace pension plans, Canada's experience has led the world — not in the direction of 'target' plans, but rather towards 'jointly sponsored plans' that provide secure and predictable defined benefits.

Canada has been a world leader in pension innovation. Pension boards, including the Ontario Teachers' Pension Plan Board ("OTPPB") and the Healthcare of Ontario Pension Plan ("HOOPP") are often cited examples of leadership in pension management and investment. The OTPP and HOOPP, along with the British Columbia Municipal Employees' Pension Plan, the British Columbia Public Service Pension Plan, the British Columbia Teachers' Pension Plan, the British Columbia College Pension Plan, the Ontario Municipal Employees' Retirement System, the Colleges of Applied Arts and Technologies Pension Plan and many others, are successful examples of a pension governance model pioneered in Canada, and now known as the "jointly sponsored defined benefit plan" (the "JSDBP") model.

PSAC members already participate in many provincially-regulated JSDBPs. In addition to the Manitoba Hospital Employees Pension Plan (HEPP), our members belong to a number of other JSDBPs, including OMERS (covering PSAC members at the Windsor, Timmins and North Bay Airports, the Port of Prescott, and Town of Moosonee), the British Columbia Municipal Plan (covering PSAC members at Victoria Airport and B.C. First Nations Health Authority) and HOOPP (covering PSAC members at the Weeneebayko Area Health Authority).

Most recently, Keith Ambachtsheer and Jim Leech have made the case for this model of pension delivery.[3]

- **JSDBPs provide secure and predictable benefits**

It is important to spotlight that the JSDBP model does not change the nature of the pension promise, nor does it undermine confidence in the pension system. Under a

[3] Memo to the Hon. Bill Morneau, from Keith Ambachtsheer and Jim Leech, March 14, 2017, Re: Time for Innovation in Federal Government-Sponsored Workplace Pension Plans, CD Howe Institute, available online: www.cdhowe.org/intelligence-memos/ambachtsheer-leech-time-innovation-federal-government-sponsored-workplace-pension.

JSDBP model, pensions are accrued with every year of service, and once accrued they cannot be reduced except in the extraordinary event of plan wind-up. JSDBPs provide decent, secure and predictable pensions and maintain pension confidence among their members — a confidence that is generally enhanced by the participation of their representatives in pension governance. JSDBPs have strengthened the pension system in Canada and continue to attract widespread support and approval from all over the world.

Solvency deficiency funding rules

The idea of changing Manitoba's solvency rules to require solvency funding only if a plan's solvency ratio is below a threshold of 85 per cent, and at the same time require enhanced going concern funding would represent a significant change from Manitoba's current requirement of solvency funding at a 100 per cent ratio level, which is intended to protect workers' future pension benefits. A number of public defined benefit plans are currently exempt from solvency requirements, as there is no reasonable prospect of plan wind-up and this exemption should be continued.

With respect to plans with solvency requirements, the government is positioning the current 100% requirement as placing an undue burden on plan sponsors, leading to the wind-up or conversion of defined benefit plans into defined contribution plans, with inferior benefits for plan members.

There is no doubt that market fluctuations have presented challenging circumstance for some pension plans with respect to solvency. However, eliminating solvency requirements altogether could open the flood gates to plans running chronic deficits, thereby putting current and future pension incomes at great risk. A better option is for the government to work cooperatively with any pension plan that may find itself in temporary distress due to market fluctuations to provide appropriate solvency relief options, subject to approval from plan members.

- **Reforming solvency funding rules**

All workplace pension plans should be 'funded' — monies should be set aside each year to pay for the pensions earned in that year, and, if there are any shortfalls in the pension plan (due, for example, to investment losses) this should be made up through additional contributions.

In Canada, we use two different sets of funding rules.

'Going concern' funding rules recognize that pension plans are long-term arrangements, and that, while investment returns and interest rates will fluctuate, there are reasonable, historically based returns and rates that can be used as a basis for funding a pension plan. Going concern funding rules are based on such long-term returns and rates, although they are also sensitive to a changing long term environment. For plans that will endure for a long time, and can absorb the volatility of financial markets, going concern funding rules are sensible ways to fund a pension plan.

'Solvency' funding rules are more problematic. They are based on the assumption that the pension plan will be terminated and wound up immediately. In this case, annuities must be purchased from insurance companies for some plan members, and actuarially determined lump sums must be paid to other members. Annuity prices are very expensive. Even though most plans won't be wound up and forced to buy annuities and make these lump sum payments, the PBA requires that all pension plans be funded on the assumption that they will terminate and wind-up, and that annuities will be purchased and lump payments will be made. This is a wholly unrealistic assumption for most plans.

The most sensible solution to the problem of termination and wind-up, when we know that some plans will terminate and wind-up but most will not, is not to compel every single pension plan to set aside enough money to cover a wind-up. This is inefficient and costly; most plans won't wind up and so won't need to be funded as though they will be wound up. Rather, the pension sector requires a government-sponsored pension insurer that will cover those plans that do wind up with a deficiency. The amount of premiums can be determined to cover expected wind-up deficits system-wide, and will cost much less than the current prohibitively expensive PBA requirement that all plans be funded on the basis that each one of them will be terminated and wound-up.

Several jurisdictions in Canada — in fact, most — have modified their solvency funding regimes to a greater or lesser extent.

In Quebec, for example, the solvency funding rule has been eliminated for all pension plans, and the going concern regime has been enhanced. We cannot summarize all the features here, but the Government of Quebec has taken bold steps to enhance going concern funding, limit the ability to apply surplus to contributions, and to provide an alternative to the wind-up procedures that may be too expensive. The rationales for these measures are to stabilize costs of pension plans and provide meaningful benefit security.

Most recently, the Ontario government has implemented more “relaxed” solvency funding requirements and required enhanced going concern funding, as well as enhancements to the Pension Benefits Guarantee Fund as a means of enhancing benefit security, as well as exploring alternatives to the wind-up procedures that are too costly.

Other provinces have also introduced “targeted solvency relief”, particularly to public and broader public sector employers, who are at lower risk of insolvency in the first place. Saskatchewan has eliminated solvency funding for major broader public sector employers, and introduced a form of enhanced going concern funding. British Columbia and Alberta have similar initiatives.

In summary, most other jurisdictions in Canada have also explored options to address level and volatility of pension plan costs through forms of solvency relief and new governance models. As we briefly mention above, one of these models — jointly sponsored and jointly governed — was originally developed in the broader public sector, and is the most successful model of pension governance and performance in Canada.

- **Priority for workers' pensions**

Over the years, we have seen companies like Nortel, and more recently Sears, put the interests of workers and pensioners at the back of the line when they go under. We encourage the Manitoba government to work proactively with other provinces, territories and the federal government to create a Canada-wide mandatory pension insurance system so that workers who have paid into a workplace pension plan are not robbed of their retirement security when companies go bankrupt.

We also ask the government to support the long overdue need for the federal government to raise the cap on defined benefit plan funding, as provided in the *Income Tax Act*, so as to allow greater flexibility to prepare for and withstand market downturns.

Locking-in provisions and access to locked-in pension funds

As a rule, workers are almost always financially better off if they leave their retirement income locked-in until retirement. This is especially true with respect to pension benefits. Unlocking retirement funds can be very dangerous, leaving workers exposed to inadequate, or even poverty-level retirement income in their later years.

The idea of loosening unlocking provisions for Locked-In Retirement Accounts and Life Income Funds in the case of financial hardship, which might include rental arrears, foreclosure and medical/dental expenses is currently being discussed.

Making it easier for workers to unlock these funds raises the likelihood that retirement income may not extend as planned through retirement. PSAC has concerns that the government's motivation for the expansion of unlocking is rooted in freeing up a larger portion of secure pension funds for access by the private investment industry and shifting financial liabilities away from government and employers.

While there may be cases of severe financial hardship which may warrant some unlocking, the risks associated with depleting one's retirement income prematurely and the required investment and financial planning knowledge required to mitigate such losses, would not be available to the average person in these situations. A better option is for the government only to permit unlocking of retirement funds in cases of extreme financial hardship and to educate working people about the financial advantages of leaving retirement funds in place for retirement.

Any changes to unlocking provisions must meet a high threshold for determining the existence of financial hardship, and labour must be a part of the determination of what constitutes financial hardship.

Moreover, in exceptional circumstances when unlocking is to be permitted, the government must provide a clear path for workers to be able to buy-back any lost time and re-qualify for future benefits. There should also be a low cap on unlocked funds so as to help ensure that workers are not sabotaged for the future.

Compulsory pension plan membership

While the government does not appear to be making an active recommendation to back away from compulsory plan membership at this time, we are concerned that they have even raised the topic for discussion. Any consideration of ripping up the long-standing principle of compulsory membership (more appropriately called automatic benefit) in workplace pension plans is absurd and grossly unfair.

Pensions are deferred earnings. They are part of a workers' overall wage package. As we have indicated earlier, pensions are crucially important to the well-being of workers and their families in retirement, and to the economic health and vitality of our communities.

RRSPs and other private voluntary schemes have proven to be severely inadequate to properly support the vast majority of families in retirement. For example, while representing 13% of all tax filers, Canadians making $80,000 or more account for more than 60% of all RRSP contributions. Mandatory pension plans are the most important vehicle to ensure that working families can retire with dignity and security after a lifetime of hard work.

Canada's unions pushed long and hard to expand the Canada Pension Plan for this reason. The CPP is not just the main way most workers save for retirement out of their employment earnings, it is the only way that millions of Canadian workers put aside a portion of their wages for retirement. While we appreciate that agreement was finally reached to enhance the CPP, very real inequities exist in the enhanced CPP agreement that will disadvantage parents who take time off to raise children – primarily women – and workers who become severely and chronically disabled.

Prior to its expansion, these two categories of workers could exclude, or "drop out" periods of low and zero earnings from the calculation of their retirement benefit. Inexplicably, these provisions were not rolled over into the recent CPP expansion. We urge the Manitoba government to take a leadership role within the country to resolve these inequities that will primarily hurt women and the disabled.

We also call on the Manitoba government to push for cross-country support to further strengthen the retirement security of all Canadians by increasing the CPP income replacement rate further, raising the ceiling on pensionable earnings and further enhancing the portion of employee contributions that are tax-deductible.

Division of pensions on relationship breakdown

Currently under the *Pension Benefits Act* when there is a court order under the *Family Property Act* or a written agreement regarding the division of family property, administrators must divide the pension or pension benefit accumulated during a marriage or common law relationship on a 50/50 basis.

This provision was put in place to try protect both spouses, and especially women who tend to have lower pensionable earnings, in their retirement. This is an extremely important objective, and any changes must include safeguards to ensure that:

- Both spouses clearly understand the full value of the pension(s) in question;
- Pension plans are required to provide pension value calculations free-of-charge to plan members; and
- Spouses are protected from being pressured, bullied or manipulated into trading pension benefits for lesser value assets, exposing them to inadequate retirement income in the future.