



**Alberta Federation of Labour**  
**Response to**  
**Report of the Alberta/British  
Columbia Joint Expert Panel on  
Pension Standards  
(November 14, 2008)**

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The Alberta/British Columbia Joint Expert Panel on Pension Standards was given a mandate by the governments of those two provinces to examine and report on ways to harmonize and modernize the pension standards legislation of the two provinces and improve access to pension plans. The Panel's 240-page report, issued November 14, 2008, contains a lengthy list of recommendations addressing both aspects of this mandate.

The Alberta Federation of Labour commends the Panel for its work and is pleased to have the opportunity to make the following comments in response to the report.

## **Harmonization and Principles-based Standards**

The Panel recommends that the two jurisdictions adopt identical pieces of pension standards legislation. While there may well be significant benefits to such harmonization, the critical (if obvious) question is the specific content of the legislation in question. Any benefits resulting from efficiency gains from harmonization might well be lost if the standards jointly prescribed are inadequate. The devil is indeed in the details, and the report doesn't provide a sufficient level of detail for us to comment.

It is suggested that this legislation should be "principles-based," rather than following the traditional rules-based design for pension standards. This proposal addresses the increasing complexity that characterizes the pension environment. New forms of pension plans are appearing, and pension standards now have to be designed taking into account their differing impacts on traditional DB plans, DC plans, multi-employer negotiated cost plans, and so on. Under the circumstances, it is suggested, principles-based pension standards might offer the flexibility that would allow regulators to deal with different kinds of pension plans in appropriate ways.

The Panel additionally recommends that the two jurisdictions "establish a joint policy advisory council and a joint pension tribunal; and work toward the establishment of a joint pension regulator for the two provinces to administer the harmonized statutes." This is a necessary corollary to the proposal for identical legislation – in the absence of such a mechanism, the cumulative impact of differing regulatory decisions would result in "regulatory drift" that would reduce or eliminate any benefit deriving from harmonized standards.

## **The AFL Response**

The advantages attributed to harmonization are, so far, hypothetical. As noted above, the real value of identical pension standards will depend on the actual content of the legislation in question. There are, however, two aspects of this proposal that cause us concern.

First, the suggested adoption of a principles-based as opposed to rules-based pension standards regime is not without significant risks. We believe that such a move could easily turn out to be, in practice, yet another form of deregulation, a policy tool that has

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not served other aspects of the financial system well. Certainly the experience of the union movement with a similar move to principles-based regulation in the field of occupational health and safety has been, from our perspective, mostly negative.

At the very least, our experience suggests that principles-based systems require a high level of regulatory oversight. Since applying principles in a wide variety of circumstances is a task more complex than simply applying clear and unambiguous rules, it requires a significant commitment of resources and a high level of training for regulators. If government fails to provide resources at the appropriate level, the regulatory system will become overstressed and if regulators don't have the required level of expertise, they may become subject to regulatory capture. In either case, the result would be negative for the pension system in the two provinces.

In the view of the AFL, the risk of this occurring is heightened by the fact that the regulator in this instance would be dependent on two governments for resources. In these situations there is a constant danger that governments may fail agree on an adequate level of resources. The two governments, after all, will be responding to different economic environments and will often have differing political and fiscal priorities.

Under the circumstances, the AFL has reservations with regard to the proposed harmonization. While we recognize that this proposal represents the core of the Panel's mandate, we also believe that it creates new risks for the pension systems of the two provinces, and promises only modest and hypothetical benefits.

### **Defined Benefit Pension Plan Surpluses**

The Panel recommends that "to overcome the impasse resulting from uncertainties about ownership of surplus in traditional DB plans," that the sponsors of these plans be allowed to "ring-fence" existing plans and their surpluses, and "to start new plans whose terms and conditions with respect to surplus entitlements would be clearly set out." In earlier consultations, the AFL has made clear its objections to any such measure. We will briefly restate our position:

1. The so-called "risk-asymmetry" argument is unpersuasive – it has failed to persuade the courts and its forceful repetition by employer sponsors and pension industry spokespersons does not convince.
2. Employer sponsors already have at their disposal many of the tools necessary to control their level of risk exposure.
3. Tilting the balance in favour of sponsor ownership of surplus creates perverse incentives within the pension regulatory environment.
4. Sponsors already have the ability to access surpluses through contribution holidays.

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5. It is not clear how the proposed changes to allow “ring-fencing” would be enacted, but workers and unions would regard any such changes as government interference in contractual relations between private parties – interference designed to favour one party at the expense of the other.

With regard to the last point, in our view such action would be illegal and would certainly be subjected to legal challenge. It is unlikely that the ensuing court actions would be resolved quickly nor would the cost to the parties involved be insignificant. We suggest that, far from reducing uncertainty, this would increase it and would also create further stress on the pension system.

Finally, the rationale for this proposal is dubious. Even a cursory examination of trends in the pension industry over the last two decades, not to mention the impact of the current economic crisis, casts doubt on the idea that, once the “impasse” is overcome and sponsors have access to surplus, employers will once again be prepared to offer new DB pension plans to their employees.

### **Other Funding Issues**

The AFL appreciates the work of the Panel in addressing funding issues, and offers at least qualified support for the following proposals:

- The continued use of irrevocable letters of credit to cover solvency deficiencies (although in the current environment these instruments may be difficult to acquire);
- Restrictions on the use of contribution holidays by employers;
- Increasing the limits on surpluses to 125% of liabilities; and
- Amending the federal *Bankruptcy and Insolvency Act* to make pension solvency deficiencies secured creditors.

### **Pensions and Financial Education**

The AFL offers qualified support for the Panel’s recommendations for increased financial education opportunities for the general public and for trustees/fiduciaries. Greater financial literacy for Canadians is a laudable goal but we offer the following cautionary observations:

1. Our school systems are already stressed meeting the many and varied educational goals we set for them. Adding another element to their mandate may create as many problems as it solves.
2. Rudimentary financial education is unlikely to equip ordinary Canadians to deal with the complexities of the financial system. Limited financial education may help reinforce Canadians commitment to savings but is unlikely to help them much in their dealings with investment issues.

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3. The main barrier to higher savings in Canada remains the stagnation of real earnings.

The Panel's recommendation that "Administrators and trustees should be required to have and use the knowledge and skills required to fulfill their obligations" is sound, as is the proposal that "Educational programs to train individuals having statutory fiduciary responsibility should be further developed and offered at the post –secondary level in both provinces." We offer, however, one qualification to this recommendation: it should not be implemented in a way that erects barriers to the participation of rank-and-file workers in the administration of their own pension plans.

## **Pension Coverage**

The Panel is to be commended for the serious attention they have given to this issue. Having said that, the AFL believes that the Panel's primary recommendation on this topic – the "ABC Plan" – has important shortcomings. Our concerns can be summarized under three headings:

1. The proposal calls for a Defined Contribution pension, with no specified benefit;
2. Participation in the plan would be optional; and
3. The contribution rates proposed may not be sufficient to support adequate retirement incomes.

The Federation of Labour urges that any new public pension be designed as a Defined Benefit (DB) rather than a Defined Contribution (DC) plan. DC pension plans lack the risk sharing/insurance feature that defined benefit plans provide and leave participants at the mercy of market volatility. That lesson has been driven home with the recent meltdown of financial and equity markets. We also believe that allowing employees and – much worse – employers to opt out means that the plan will not achieve the uptake its proponents expect.

The Panel suggests that the way to get around the problem of low uptake is to design the plan to feature "auto-enrollment" – in other words, employees and employers are automatically in the plan unless they make the effort to opt out. The hope is that this will boost participation in the plan far enough to make a meaningful improvement to pension coverage.

This argument is difficult to accept. Based on a logic similar to the "negative option marketing" employed by TV cable providers, it assumes that most people enrolled (or rather, auto-enrolled) will either like the plan or be too indifferent to bother opting out.

Worse yet, a closer examination of the report reveals that employees and employers do not have equal opt-out rights. The report says that:

*The Panel advocates making participation compulsory for employees of employers who participate in the plan. We recognize that this poses the risk*

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*that a group of reluctant employees could persuade an employer to opt out, but we believe that this requirement would greatly improve participation.<sup>i</sup>*

This last remark misses the point. If employers can compel workers to participate in the plan but workers don't have a similar ability to compel employer participation, the auto-enrollment aspect of the plan will be perceived as fundamentally unfair. This is especially likely since the report also states:

*If the employer opts out, each employee would still be automatically enrolled without employer contributions (emphasis added) unless he/she opted out (a double opt-out concept)<sup>ii</sup>*

Further, it is difficult to believe that the auto-enrollment feature will lead many employers to participate in a meaningful way. The Panel suggests that:

*Employers in our provinces would, we suggest, welcome such an ABC Plan provided it could truly deliver on the key objectives noted above. Many employers find the administration of a pension plan a distraction from their primary goal of delivering goods and services to their customers. We submit that the notion that employers believe they must provide a pension plan as an attraction and retention tool has significantly less merit today than it once had due, in part, to the fact that the time and resources required by employers to provide pension plans, coupled with the increasing regulatory complexity and liability associated with these plans has made this unilateral decision to provide a pension plan one which many employers wish to avoid or off-load. This is not to suggest that employers in our provinces do not wish to ensure that employees are saving for and have adequate retirement income as clearly the submissions we received indicate employers care deeply about providing for and assisting their employees with retirement savings.<sup>iii</sup>*

Frankly, the AFL is skeptical about these assertions. An employer who is not already offering a pension of some kind to employees is likely unwilling to bear the expense of contributing at a meaningful level, and will therefore probably choose to opt out of the ABC Plan unless, of course, participation can be done at a very low cost.

This highlights yet another problem with the ABC Plan. The report suggests a three-tiered contribution structure. Tier A would require 3% of earnings to be contributed by each of the employee and the employer. Tiers B and C would feature "contribution formulas of six and six percent and nine and nine percent respectively." The first two of these contribution rate structures are utterly inadequate. At best, they would provide employees with a false sense of security, while failing to provide a retirement income adequate to prevent poverty in retirement. Even the highest contribution rate formula (9% and 9%) might prove inadequate in a period of low market returns and low interest rates and one has to question how many employers who are currently unwilling to provide an occupational pension plan would be willing to participate in the ABC plan at a 9% increase in payroll costs.

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Finally there is a danger that, far from increasing pension coverage, the ABC Plan could undermine existing plans. Employers who want to shed the costs and risks of existing occupational pension plans may seize the opportunity to move to the ABC Plan. Unless employees are provided with expert and impartial financial and technical advice, they may well be persuaded to acquiesce to such a move, a move that could be to their financial detriment.

On balance, the AFL believes that the proposed ABC Plan would be unlikely to significantly improve pension coverage in Alberta and would be unlikely to provide adequate retirement incomes. If the looming crisis in retirement incomes in Canada is to be addressed, any proposal for a new public pension plan should have two characteristics:

1. A contribution and benefit structure that would provide for an appropriate lifestyle on retirement; and
2. Compulsory participation for all employers and employees except in cases where an existing occupational pension provides equivalent or superior benefits.

In our view, the policy instrument that would best meet these criteria is a supplement to the existing Canada Pension Plan. Participation in this supplementary plan would be mandatory for employers, exempting only those that offer a work-based pension that is actuarially equivalent to or better than the enhanced CPP.

The Supplementary CPP would feature low administration and investment costs and would effectively provide a predictable and reliable retirement income for Canadians.

## Conclusion

The AFL thanks the members of the Joint Expert Panel on Pensions for their work. We recognize that the issues and the pension environment are complex, and pose difficult problems for policy-makers. Our response to the Report, while critical in several respects, is tendered in the spirit of constructive dialogue. Only through such a dialogue can we hope to progress, and to protect the retirement incomes of Canadians.

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<sup>i</sup> *Getting Our Acts Together*: report of the Joint Expert Panel on Pension Standards, p.186

<sup>ii</sup> Ibid

<sup>iii</sup> Ibid, p.183