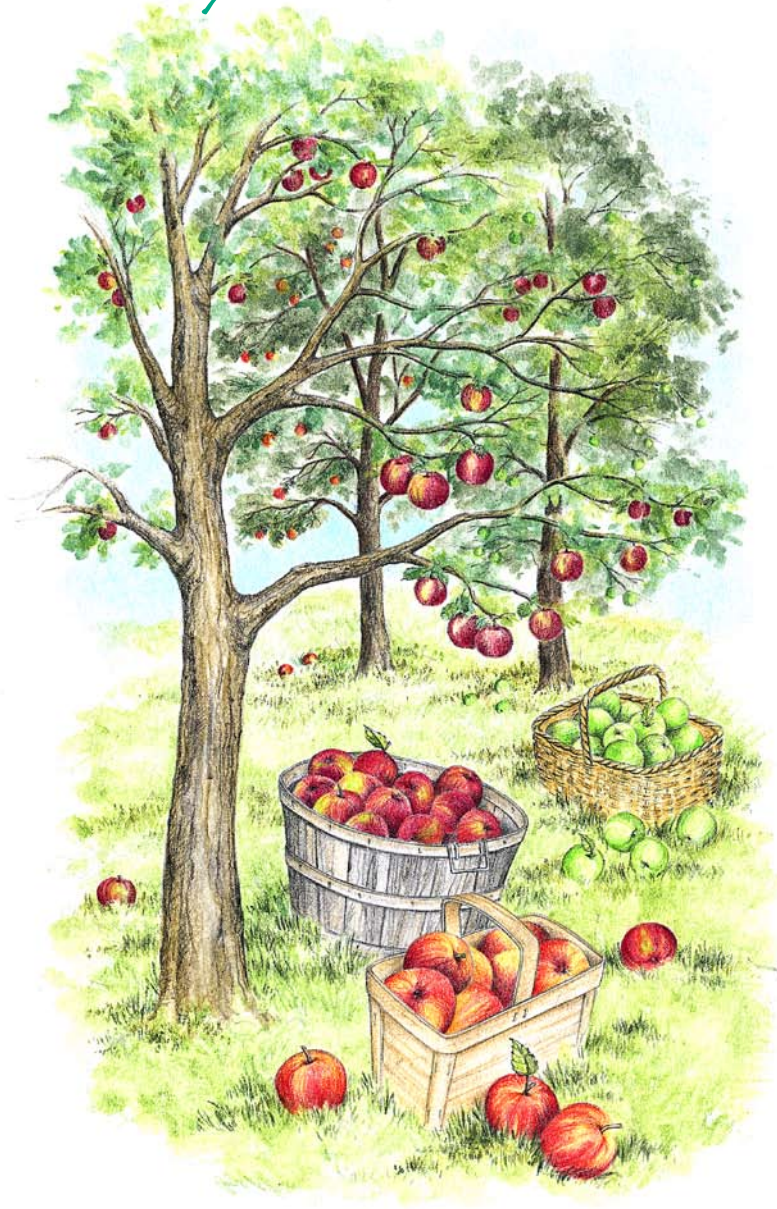


Régie des rentes du Québec

Supplemental Pension Plans

# Sound administration

*what you should know*



Québec 

## **Acknowledgements**

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This publication does not have force of law. In cases of conflicting interpretation, the *Supplemental Pension Plans Act* and its regulations prevail over the contents of this publication.

This document is also available for downloading on the Web site of the Régie des rentes du Québec ([www.rrq.gouv.qc.ca](http://www.rrq.gouv.qc.ca)).

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# Sound administration

## *What you should know*

For many workers who are members of supplemental pension plans, such plans represent the main source of income after retirement. Therefore it is important that pension committees<sup>1</sup> ensure sound administration so as to protect the rights of their members and beneficiaries.

The Régie des rentes du Québec—along with a number of others in the pension field—has observed shortcomings in the administration of pension plans. In some cases, these shortcomings can involve the personal liability of pension committee members. Here are some examples:

- The pension committee members meet only once a year, before the annual meeting;
- The pension committee delegates duties<sup>2</sup> but does not follow through;
- The measures for internal control are inadequate for ensuring that contributions are paid every month to the pension fund;
- A single committee member makes the decisions and monitors the plan's administration;
- Certain committee members act so that the interests of one particular group take precedence over the best interests of the plan's members and beneficiaries;
- Certain committee members lack information and training for properly exercising their role.

Plan administration must be organized so that the pension committee can carry out its duties in a competent and prudent manner. This is why it is necessary to establish rules for sound administration. All the members of the pension committee must be familiar with the rules and apply them.

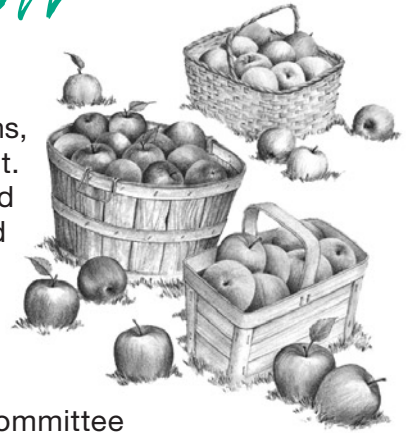
This first instalment will deal with the sound administration of a pension plan and present the basic principles. You will find eleven rules aimed at helping you establish procedures for sound administration.

A self-evaluation is also provided so you can determine whether you administer your pension plan well.

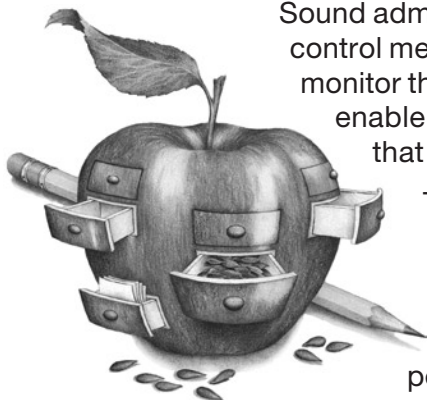
The principles and rules presented in this instalment constitute the basis of sound administration. The mechanisms that must be developed for respecting those principles and rules vary according to the specific characteristics of each plan. We suggest that you familiarize yourself with the principles and rules in order to set up rules that will be well-adapted to your pension plan.

<sup>1</sup> If a pension plan has less than 26 members, the employer can take the place of the pension committee.

<sup>2</sup> In this issue, the term “delegate” means to confer duties.



## What is sound administration?



Sound administration is achieved when a set of procedures and internal control mechanisms are put into place to manage the pension fund and monitor the day-to-day administrative activities. Those procedures will enable the pension committee to respect the principles and rules that must guide it in properly administering a pension plan.

The procedures will be applied by the pension committee and others involved in the plan's administration: the employer, financial institutions and consultants. These are the **key players** in plan administration because they perform a number of financial and administrative duties for the pension committee.

Sound administration reflects the ethical values of the pension committee. It allows for appropriate action to be taken in different situations. The motivation and involvement of pension committee members are part of sound administration and they foster collaboration and communication.

### The advantages of sound administration

Sound administration entails numerous advantages, thus facilitating:

- decision-making
- satisfactory monitoring of the plan's administration
- a better control of risks
- the division of responsibilities among the various players
- accountability
- the performance assessment of key players
- etc.

In addition, sound administration prevents:

- investments that are contrary to the investment policy
- contradictions between the plan text and the administrative practices
- breaches of the *Supplemental Pension Plans Act*
- a lack of information and training on the part of pension committee members
- charging inappropriate expenditures to the plan
- fraud
- conflicts of interest
- insufficient information for members and beneficiaries
- etc.

In other words, sound administration promotes good plan administration, increases the confidence that members, beneficiaries and the sponsor have in the pension plan and contributes to minimizing the risk of mistakes.

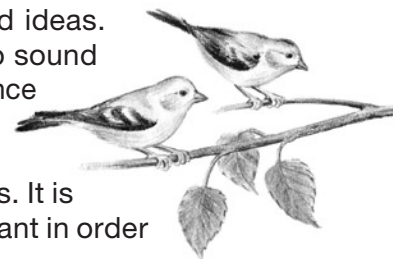


## The basic principles of sound administration

Administering a pension plan resembles administering a business. Like any person who is responsible for administering property that is not his or her own, a pension committee must act in a competent and prudent manner. To do so, it is necessary to respect the following six basic principles of sound administration.<sup>3</sup>



- **Openness** allows for the complete reality of a situation to be seen in an unembellished, impartial manner. Given that the pension committee must exercise powers on behalf of others, it must be accountable for its actions. Openness is achieved through ongoing, open communication between the parties to the pension plan and the others involved.
- **Continuity** ensures uninterrupted administration. Thus, the committee takes steps to preserve the pension plan's documents (for example, rules are determined for the transfer of the plan's data in the case of a change of actuary or fund manager), to prepare for changes in the committee's membership and to ensure the pension plan's short- and long-term financial security.
- **Efficiency** is achieved when you obtain results with minimal use of resources. It is the outcome of systematically seeking to optimize financial, material and human resources, which must not be done at the expense of the parties to a retirement plan. Furthermore, the administration costs must be proportional to the size of the pension plan.
- **Balance** refers to the right mix of opposing strengths and ideas. The harmony resulting from that equilibrium contributes to sound administration. The pension committee demonstrates its balance by exercising its powers and by means of the fair choice of means available to it for reaching its objectives. To act with prudence, the committee must consider potential risks. It is not necessary to systematically ask the advice of a consultant in order to act in a manner that is judicious.
- **Integrity (probity)** for a pension committee member means renouncing any advantage or interest that is not contractually granted to him or her in the exercise of his or her duties. In addition, a pension committee member cannot place himself or herself in a real or potentially conflictual situation between his or her own interests and those of the members and beneficiaries.
- **Fairness** implies equal and impartial treatment of the group of members, beneficiaries and key administrative players.



Those principles must serve to guide the pension committee, regardless of the type of plan (defined benefit or defined contribution), its size or the structure of its administration. Only the specific procedures and tools differ according to the characteristics of each plan. Thus, there is generally not a subcommittee for monitoring investments in a small plan.

<sup>3</sup> Based on the book *Exercer la saine gestion, Fondements, pratiques et audit*, by Bernard Brault, CCH, 2002.



## Eleven rules for establishing procedures for sound administration

The following eleven rules are intended to help the pension committee establish procedures for sound administration that promote openness, continuity, efficiency, balance, integrity (probity) and equity in the administration of a pension plan.

You can also consult the document entitled *Pension Plan Governance* published by the Canadian Association of Pension Supervisory Authorities (CAPSA).

### 1. Have a good understanding of your role and responsibilities

When a new committee member is designated, the pension committee provides him or her with information on:

- the role and responsibilities of the pension committee and its members
- the operations of the pension plan and its administration
- the administrative objectives and issues
- available training

In addition, it is important that committee members have access to all the pension plan documents (see question 2 of the self-evaluation that follows this document) and that they understand the content.

An employer that acts as a pension plan administrator has the same obligations as a pension committee. The employer's agents must also know their duties and the manner in which they must be carried out.

### 2. Establish rules of conduct

The pension committee—as well as each of its members—must act in the best interests of the members and beneficiaries. To this end, the committee should adopt a code of ethics to ensure, among other things, members' honesty, loyalty and integrity.

With a code of ethics in place, pension committee members will:

- avoid acting in their own interest or placing the interests of one group above another;
- know whether they have the right to accept gifts and other advantages, and to what extent, etc.



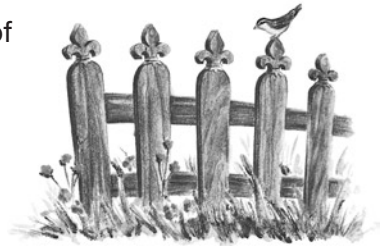
## Example

*Pension committee members have to make decisions about investing the pension plan's assets. Investments that involve greater risk may allow the pension plan sponsor to reduce its contributions. However, that cannot be the main criterion in deciding. Rather, the committee must consider the best interests of the members and beneficiaries as a whole. If several members are near retirement, such investments may not be appropriate.*

### 3. Separate day-to-day administrative activities from management functions

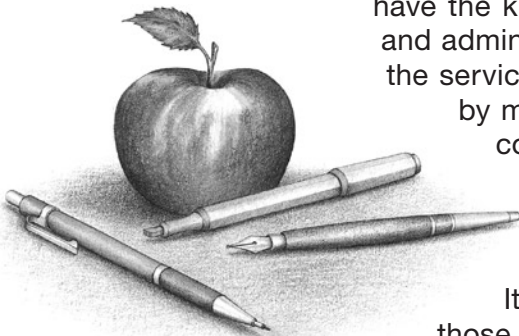
The role of a pension committee can be compared to that of a board of directors in a business. The committee makes strategic decisions, conducts risk control and monitors the administration.

In order to perform its role objectively and with openness, it can assign the direction of day-to-day activities to a third party, such as an employer representative, an outside consultant or a financial institution.



### 4. Delegate functions to capable persons

Pension plan administration is complex. Pension committee members do not necessarily have the knowledge required for carrying out certain financial and administrative functions. The committee can therefore use the services of capable persons. It can assign such functions by means of a mandate, delegation of powers or service contract.<sup>4</sup>

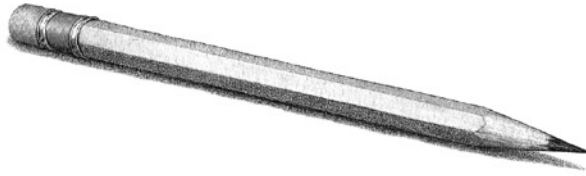


The committee must be sure to assign those functions to capable persons, which it can do by holding a call for tenders and specifying the selection criteria.

It is also important to verify the work methods used by those persons. This can involve verifying the practices of the consultant responsible for ensuring that amendments to the plan are in conformity with applicable legislation.

<sup>4</sup> The distinctions between these types of contract are set out in the *Guide for Pension Committee Members* published by the Régie des rentes du Québec.

## 5. Specify the roles and responsibilities of those involved



When the pension committee delegates functions, it must specify the nature of those functions. Thus, each person involved knows his or her responsibilities. Consequently, if a person carries out more than one role, he or she will be able to distinguish the limits of each role.

The management of current operations is often assigned to a representative of the employer who also sits on the pension committee. That person therefore assumes two roles, in which case it may be difficult to know in which capacity he or she is acting. This, in turn, can lead to overstepping the mandate.

In the case of a plan that is administered by the employer, clear rules should also be established to separate the employer's functions according to whether it involves acting in the capacity of administrator or employer. When the employer makes a contract on behalf of the pension plan, the employer should sign it as administrator and not as the employer.

### Example

*The responsibility for calculating pension benefits was entrusted to the director of human resources, the representative of the employer. A member who was dissatisfied with the amount of his pension, complained to the director of human resources, who, in turn, was also a member of the pension committee. After reviewing the member's file, the director refused to increase the member's pension.*

*The member asked the director to forward his complaint to the pension committee. The director refused, pointing out that the decision he had reached was rendered on behalf of the pension committee. The director did not inform the pension committee members about this matter. Subsequent to representations made by the member, the plan actuary informed the pension committee members that the member's complaint was founded.*

*To avoid such a situation, the committee could have:*

- *specified the nature and limits of the mandate (the director did not have the power to respond to complaints on behalf of the pension committee);*
- *put into place a policy for handling complaints that foresees the possibility that the actuary may revise the calculation of the pension.*

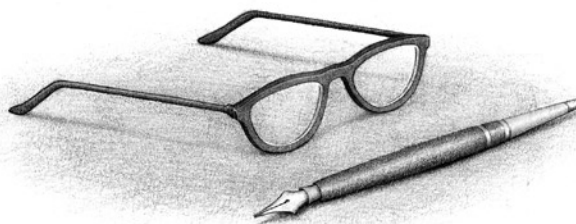


## 6. Put into place monitoring mechanisms

The pension committee has the ultimate responsibility regarding administration of the pension plan. When it delegates functions to other persons, it must put into place monitoring mechanisms to ensure that the work is properly carried out.

Such mechanisms will allow the committee to monitor, among other things:

- pension fund performance
- payment of contributions
- cash outflows and administration costs
- the plan's conformity with laws and regulations



Monitoring can be carried out by various means. The nature and frequency with which information and reports are provided to the committee must be specified. For example, the committee may require the person responsible for enrolling members who are eligible for membership in the plan, to attest, within a prescribed period of time, whether that duty has been properly fulfilled.

Failure to establish adequate monitoring rules may result in liability on the part of pension committee members.

### Example

*In a small city<sup>5</sup>, the treasurer made investments that were not proper and that caused the plan to lose 2.5 million \$ in six months. The chief administrative officer (CAO), acting as administrator of the pension plan, was held personally liable for the damages.*

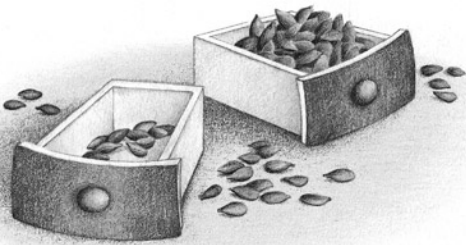
*The Court was of the opinion that the CAO was grossly negligent. He had neglected his fiduciary duties.*

- *He failed to implement internal control procedures for verifying investments;*
- *he placed blind faith in the treasurer without reading the documentation provided by the fund manager and accepted vague answers.*

*The lesson applies to everyone. If the pension committee had established rules for verifying the conformity of investments and the information provided by the treasurer, it is quite possible that it could have avoided or put an end to this situation.*

<sup>5</sup> For further information, see the decision in *Remmers v. Lipinski* (2000) A.J. No. 362 (Court of Appeal of Alberta, 31 March 2000).

## 7. Evaluate the performance of key players



The committee must regularly evaluate the performance of its consultants and those who carry out financial and administrative duties. When the committee lacks the required competence, it can call upon experts.

Performance appraisals must rely on quantifiable and reasonable criteria, as well as on impartial assessments. The committee may require that the statements of end of participation be provided within 30 days of the date on which it has learned that a member has ceased being an active member, even if the law allows for a 60-day period in which to provide such a statement. Failure to respect that deadline may indicate a breach.

## 8. Require good information and promote the acquisition of knowledge

The pension committee members and key players must have good information that is up to date and accurate, including the most recent version of the plan's text.

In addition, pension committee members must understand the information provided to them. Trusting is not enough! Too often, the pension committee accepts vague answers such as "I've always done things that way...it's never been a problem."

The committee must be able to detect problems, make good decisions and adequately monitor the plan's administration. To that end, the committee needs plans for training its members.

## 9. Control risks

Mechanisms must enable the committee to rapidly detect risks, to evaluate their extent and to take action. The committee could require that the employer provide, on a monthly basis, a confirmation attesting to the payment of contributions.

The following is a list of some of the risks to which a plan may be exposed:

- the non-payment of contributions
- the decline in value of pension fund investments
- an investment policy that is not adapted to the plan's maturity
- the deterioration of the employer's financial situation
- an unjustified increase of administrative and management costs
- a plan whose administration is not properly supported by its computer and administrative systems
- an insufficiently diversified choice of investments offered to members of a defined contribution plan



## 10. Foster communication and pension committee accountability



Administrative openness depends largely on the exchange between the various players, members and beneficiaries.

The pension committee must establish policies for informing the members and beneficiaries about the plan's administration, their rights and obligations, as well as any important event. It should also specify how to make a request or a complaint.

Communications are important because they enable the pension committee to regularly report on the plan's administration rather than only at the annual meeting. This results in members and beneficiaries having greater confidence and interest in their pension plan. For example, in certain plans, members are regularly informed via an intranet as to the plan's terms and administration, the evolution of the pension fund's performance, the arrival of a new pension committee member, etc.

On the other hand, it is also important to foster communication between the pension committee, the plan sponsor<sup>6</sup> and the key administrative players, because they all work together and actively collaborate on achieving the objectives of the pension plan.

## 11. Evaluate your rules for sound administration

The pension committee should regularly evaluate the effectiveness of existing management procedures and mechanisms in order to make the necessary changes. In turn, it should inform the members, beneficiaries and the employer.



***You now hold the keys to the sound administration of a pension plan. We invite you to complete the attached self-evaluation in order to see how the administration of your plan rates. Some of the information may help you put in place rules adapted to your needs.***

<sup>6</sup> Generally, the employer and, in some plans, the union.

# Self-evaluation

This self-evaluation is intended to help the pension committee determine whether it applies the rules for sound administration of a pension plan.

## General questions

	yes	no
1. Have you had any training for fulfilling your duties as a pension committee member?	<input type="checkbox"/>	<input type="checkbox"/>
2. Do you have access to all the documents related to the pension plan and its administration? These would include:	<input type="checkbox"/>	<input type="checkbox"/>
a) the plan text and its amendments	<input type="checkbox"/>	<input type="checkbox"/>
b) the annual information return (federal, provincial)	<input type="checkbox"/>	<input type="checkbox"/>
c) the plan's financial statements	<input type="checkbox"/>	<input type="checkbox"/>
d) the investment policy, if applicable <sup>7</sup>	<input type="checkbox"/>	<input type="checkbox"/>
e) the actuarial valuation (defined benefits plan)	<input type="checkbox"/>	<input type="checkbox"/>
f) administrative procedures (written policies, guidelines, administrative manuals)	<input type="checkbox"/>	<input type="checkbox"/>
g) pension committee bylaws	<input type="checkbox"/>	<input type="checkbox"/>
h) contracts for various associates (mandate, delegation, service contract)	<input type="checkbox"/>	<input type="checkbox"/>
i) supporting documents related to administration costs	<input type="checkbox"/>	<input type="checkbox"/>
j) consulting reports and opinions	<input type="checkbox"/>	<input type="checkbox"/>
k) the minutes of pension committee meetings	<input type="checkbox"/>	<input type="checkbox"/>
l) the minutes of annual meetings	<input type="checkbox"/>	<input type="checkbox"/>
3. Are you informed of the delegations made by the pension committee?	<input type="checkbox"/>	<input type="checkbox"/>
4. Do you believe that the pension committee's rules for internal management are adequate to enable you to carry out your duties?	<input type="checkbox"/>	<input type="checkbox"/>

<sup>7</sup> In a defined contribution plan in which members decide on the investments of their contributions and those of the employer, the pension committee is not required to establish a written investment policy.

## Specific questions

yes    no    I don't  
know

### The division of responsibilities among the various associates

- |  |                          |                          |                          |
|--|--------------------------|--------------------------|--------------------------|
| 5. Are you informed of the responsibilities of each associate?                                       | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| 6. Do you know whether those people act as mandataries or as delegates?                              | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| 7. Are there mechanisms in place for monitoring the work of these persons (reports, meetings, etc.)? | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| 8. Does the pension committee regularly evaluate the performance of key administrative players?      | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

### Monitoring of the plan's conformity and risk management

- |   |                          |                          |                          |
|---|--------------------------|--------------------------|--------------------------|
| 9. Are there mechanisms for ensuring that the plan is in conformity with legislation?   | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| 10. Are there mechanisms for ensuring that the plan is administered in conformity with the pension plan text?                                 | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| 11. Are there mechanisms for rapidly detecting various risks?   | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| 12. Is the investment policy thoroughly reviewed on a regular basis (it is recommended that it be reviewed every 3 to 4 years) <sup>8</sup> ? | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

**If you administer a defined contribution pension plan in which members decide on the investment of their contributions and those of the employer, skip to question 15.**

- |   |                          |                          |                          |
|---|--------------------------|--------------------------|--------------------------|
| 13. Are there any particular events that require a special review of the investment policy, despite the fact that it is regularly reviewed?   | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| 14. Are there rules for monitoring the performance of the pension fund and the conformity of investments (for example, does a subcommittee study the manager's reports)? <sup>9</sup> | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

<sup>8</sup> Pelletier, Jean-Jacques and Normand, Carmand. *Caisses de retraite et placements : introduction à la gestion des placements*, Sciences & culture, Montréal, 1994, p. 374.

<sup>9</sup> Such rules are generally established for large pension plans that conduct active management.



- |   | yes                      | no                       | I don't<br>know          |
|---|--------------------------|--------------------------|--------------------------|
| 15. In the case of a defined contribution plan in which members make the investment choices, is there monitoring of the overall performance of investments? | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

### The pension committee's internal bylaws

- |  |                          |                          |                          |
|--|--------------------------|--------------------------|--------------------------|
| 16. Does the pension committee have rules for dealing with:  |                          |                          |                          |
| a) the development of members' skills (training and information pertinent to fulfilling their responsibilities)? | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| b) the division of responsibilities between members?   | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| c) conflicts of interest and ethics?   | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

### Communications

- |  |                          |                          |                          |
|--|--------------------------|--------------------------|--------------------------|
| 17. Are there rules guiding the communication of information about the plan and its administration to members and beneficiaries? | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| 18. Is there a written policy for handling complaints from members and beneficiaries?  | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

If you answered “no” or “I don't know” to any of the questions, we recommend that you discuss those questions at an upcoming meeting of the pension committee and review, if needed, the operating rules that guide the administration of your pension plan.

### Remember, slow and steady wins the race!

*If your plan is not administered by rules of sound administration, don't try to change everything all at once. Take the time to put sound administration practices into place, one sector at a time. You can start with financial functions and then follow with administrative functions, communications, etc. What counts is ensuring that all involved—including members and beneficiaries—are informed of the work plan and its progress.*