FAQs about actions taken by OSFI in connection with Air Canada's Pension Plans

Under the *Pension Benefits Standards Act, 1985* (PBSA), the Office of the Superintendent of Financial Institutions (OSFI) has the responsibility to supervise federal private pension plans to determine whether they are meeting regulatory requirements and, in doing so, to strive to protect the rights and interests of the members, retirees and other beneficiaries.

OSFI has been and will continue to work in accordance with its mandate and will work with plan administrators and others to provide information to plan members, retirees and other beneficiaries and to help minimize the uncertainty that they may be experiencing.

You may also wish to visit the Air Canada Web site (www.aircanada.ca). In the "What's New" section, there is a new page called Air Canada Restructures. The Court affidavit filed on April 1, 2003, by Air Canada is posted there. Pages 31, 32 and 33 make reference to pension issues.

The questions and answers that appear below reflect the general kinds of questions OSFI receives through its 1-800 line, its Web site and from the news media. These will be updated as appropriate.

I. OSFI's Role and Actions

Q1. Why did OSFI let the plans deteriorate to this extent?

A1. The prime responsibility to manage the plans rests with the plan administrator (Air Canada). As of 2001, the plans had a surplus of approximately $915 million. Going into 2002, OSFI's assessment was that the plans did not have a significant deficit. OSFI's stress testing in early 2003 identified the possibility of a material deficit, which was confirmed with the company. That led to the range of actions identified in Q2, below.

Q2. What actions did the Office of the Superintendent of Financial Institutions (OSFI) take in respect of the Air Canada pension plans?

A2. OSFI raised the issue with Air Canada management early in 2003 to see if pension-funding issues could be addressed in a timely manner. Subsequently, OSFI required that approximately $200 million be put into the plans over a period of time to cover current service costs for 2002-2003. OSFI also accelerated the timing of reports to valuate the pension plans in order to verify the extent of the funding shortfalls. Finally, OSFI also required Air Canada to communicate with plan members and retirees on the financial status of the plans.

Q3. Did OSFI's actions cause Air Canada to file for CCAA in Canada and Chapter 11 in the United States?

A3. No. Prior to Air Canada deciding to file under the CCAA in Canada and Chapter 11 in the United States, OSFI had accepted a proposal under which the company would provide funding to its pension plans. Subject to Air Canada's confirming its willingness to proceed with the proposal, OSFI would have been willing to put regulatory action on hold. OSFI continues to be open to working with the company on funding arrangements and restructuring of the pension plans.

Q4. What are you doing to make plan members , retirees and other beneficiaries aware of the status of their pension plans?

A4. OSFI has instructed the Air Canada plan administrator, who is responsible for communication with plan beneficiaries, to convey information regarding the financial status of the plans to plan members, retirees and other beneficiaries, which is now occurring. OSFI has the authority to order that more information be provided to plan beneficiaries, if we deem this to be appropriate.

Q5. What does OSFI do to protect members, retirees and other beneficiaries of an under-funded pension plan?

A5. Defined benefit plan sponsors are required to pay current service costs and to fund any deficit in the plans.

Plan administrators must submit valuation reports to OSFI at least every three years indicating the funded status of the plan. OSFI has the authority to ask for valuation reports at any time, in the event that doing so appears warranted. This is generally the same approach followed by provincial pension regulators.

If a valuation report indicates that a plan is under funded, the administrator must fund the plan by making special payments over a five-year period. As well, an under-funded plan is required to file a valuation report every year until the plan no longer has a deficit.

Q6. Why doesn't OSFI require a valuation report more often than every three years?

A6. The plan administrator must submit valuation reports to OSFI every three years, indicating the funded status of the plan. This is the same general practice followed by other pension regulators in Canada. However, OSFI has the authority to ask for valuation reports at any time if it feels that the circumstances of the plan require an updated valuation.

Q7. OSFI directed Air Canada to file new valuation reports in a letter sent to the company on March 21, 2003. Has Air Canada filed those reports with OSFI?

A7. On Friday, May 2, 2003, Air Canada provided nine reports (related to ten plans) that show an update on the financial position of each plan as at year-end 2002 or January 1, 2003. Although the information received is not sufficient as the reports do not include the required payment schedule, OSFI has informed Air Canada that its obligations under the PBSA still applies, including the funding requirements of the PBSA, and that these amounts continue to accrue to the pension plans.

Plan members, retirees and other beneficiaries can view this information on request to the plan administrator.

II. The Impact of CCAA

Q1. Since Air Canada is now operating under CCAA, what does it mean to me as a pension plan member?

A1. In general, going under CCAA means a company is attempting, under a court-supervised process, to restructure its operations, which, if successful, would allow it to continue to operate. At the moment, this means that payments to the plan are on hold. The administrator, which is Air Canada, will continue to administer the plan and detailed questions should be addressed to them.

Pension fund assets are held separately and can't be used to deal with other financial obligations of Air Canada.

Q2. Seeing Air Canada has filed for CCAA, can they shut down the pension plans?

A2. This is a restructuring under the CCAA and not a bankruptcy. In Air Canada's court filings, the company indicated that it does not plan to immediately wind up the plans. However, they may wish to restructure them. This would require negotiations with representatives of employees, as well as OSFI's authorization.

Q3. I saw a newspaper article that says that Air Canada has the right to withhold my pension plan payments under the terms of the CCAA filing the company made. Is this true?

A3. No. The CCAA filing pertains only to the company and its assets and liabilities. The funds in the pension plan are held separate and apart and have nothing to do with the CCAA filing.

Q4. Can the company reduce the amount of benefits I am receiving?

A4. In order to change the amount of benefits you are receiving, the company would have to restructure the plans. Such restructuring should involve negotiations with the various employees' unions. Any restructuring that reduces accrued pension benefits would also require the OSFI's authorization.

Q5. If CCAA is not successful and Air Canada goes bankrupt, what happens to its pension funds?

A5. Pension funds are not an asset of the company. They would be distributed in accordance with the plan text and the *Pension Benefits Standards Act* (PBSA) *1985*. Some examples of the kinds of points that would be contained in a plan text include: the formula for determining pension benefit levels; any type of distribution scheme that would determine priority for distribution of assets on termination of the plan. The PBSA requires that on termination of a plan, all benefits become vested, which means that plan members become entitled to a benefit regardless of their length of membership in the plan. The valuation of the liabilities in the plan must meet the minimum standards of the Act, for example the provision of spousal benefits must be honoured. An administrator would continue to be responsible for the plan, and OSFI would be required to approve distribution of pension assets.

Q6. On April 22, OSFI announced its intention to file a motion to alter certain elements of the protection order covering Air Canada under the *Companies' Creditors Arrangement Act* (CCAA). Why is OSFI taking this step at this time?

A6. As supervisor of all federally regulated pension plans, OSFI's mandate is to safeguard pension plan members, retirees and other beneficiaries from undue loss. In keeping with this mandate, OSFI intends to apply to amend specific elements of the initial court order regarding the restructuring of Air Canada.

Specifically, the initial order did not distinguish between Air Canada's obligations to its pension plan members, retirees and other beneficiaries and claims made against the company by other creditors. OSFI believes that amounts due to pension funds are not subject to the CCAA restructuring process and should move ahead of other creditors. OSFI also believes that Air Canada should resume making regular contributions to the plans.

As well, OSFI wants to clarify the initial order with respect to the agency's ability to take certain regulatory action. Outstanding is a requirement that Air Canada provide, by April 30, 2003, updated valuation reports for all of its pension plans, as of January 1, 2003. This is designed to confirm the extent of the shortfall in the plans and establish the level of current contributions required under the new valuations.

III. Other Issues

Q1. If the company does end up failing and if a portion of the company is sold to another organization, what happens to the pension plans?

A1. To try to provide a generic answer is not easy because too many factors could come into play. For example, if one company were sold to another company, the purchaser might not wish to assume the responsibility for the other company's pension plan obligations. In such a case, the selling company's plan might be terminated, in whole or in part, and the assets distributed amongst the plan members, retirees and other beneficiaries. In another scenario, the acquiring company could decide to assume the obligations of the other company's pension plan, in which case OSFI's approval must be obtained for the transfer of the assets and liabilities to the purchaser's pension plan.

Q2. If another company were to buy a portion of Air Canada, would they be responsible for maintaining the same pension plan or could the plan's rules or the company's contributions change?

A2. In general, there would be no obligation to maintain the terms of the original plan. To try to provide a generic answer is not easy because too many factors could come into play. For example, if one company were sold to another company, the purchaser might not wish to assume the responsibility for the other company's pension plan obligations. In such a case, the selling company's plan might be terminated, in whole or in part, and the assets distributed amongst the plan members, retirees and other beneficiaries. In another scenario, the acquiring company could decide to assume the obligations of the other company's pension plan, in which case OSFI's approval must be obtained for the transfer of the assets and liabilities to the purchaser's pension plan.

Q3. I am only months away from retirement. What happens if Air Canada goes bankrupt before I reach official retirement? Will I still receive a pension?

A3. Your benefits would be calculated in accordance with the terms of the plan and distributed to you. If the plan is terminated in a deficit position, the exact level of benefits would not be known until a final accounting of all the assets and liabilities of the plan are known. This can take many months to determine, depending on the size of the company and the number of plan members, retirees and other beneficiaries. This is because it is necessary for the plan actuary to collect and verify all relevant information about plan members, retirees and other beneficiaries (e.g. length of service, amount of personal contributions, etc.).

Q4. How long might it take for me to actually receive my benefits?

A4. The plan administrator would be in charge of the process and has a responsibility to make the payment of benefits as quickly as possible. Those already receiving pension benefits are expected to continue to receive payments. However, it may be necessary for the administrator to reduce the amounts until the full accounting of assets and liabilities has been determined.

Q5. If Air Canada goes bankrupt, are members, retirees and other beneficiaries of the pension plan entitled to both employee and employer contributions?

A5. Yes. Under the terms of the PBSA, pension fund assets, whether by the employer or the employee, are held separate and apart from the corporate assets.

Q6. If pension plan members, retirees and other beneficiaries are treated the same as creditors in the event of an Air Canada bankruptcy, what can OSFI do to help them recover the funds?

A6. Pension plan members, retirees and other beneficiaries are not treated as creditors – pension plan assets are separate from company assets and the entitlements of plan members, retirees and other beneficiaries would be based on a valuation of the assets in the plan compared to its liabilities. In addition, the pension plan would continue to be overseen by an administrator who would determine any additional actions in respect of the plan. The administrator would be responsible for making any additional claims on the estate of the company in an attempt to recover the shortfall.

Q7. If Air Canada goes bankrupt with unfunded liabilities, do the pension plan members, retirees and other beneficiaries fall in line with creditors for the shortfall? If so, does that mean they may never receive their money?

A7. The entitlements of members, retirees and other beneficiaries would be based on the value of the pension plan assets versus its associated liabilities. If the plan is under funded, generally this would mean that members, retirees and other beneficiaries would receive only a portion of their benefits. The amount would depend on factors such as the extent of the deficit in the fund and whether the terms of the plan give priority status to certain classes or types of members, retirees and other beneficiaries.

Q8. Is there a guarantee fund for pension plans?

A8. Not at the federal level. Only the Province of Ontario offers guarantee insurance for provincially regulated pension plans.

Q9. Why is there no guarantee insurance at the federal level?

A9. Fundamentally, pension plans represent an agreement between the employer and its employees and the federal government has no role to play in backstopping private sector arrangements.

Q10. Since companies invest pension fund monies in stock markets, are there any federal regulations that govern the types of investments that plan administrators can make with pension fund assets?

A10. Both the *Pension Benefits Standards Act (PBSA)* and the *Pension Benefits Standards Regulations (PBSR)* set out requirements for plan administrators that apply to all investments of a pension plan, including those made in equity markets.

The *PBSA* requires plan administrators to exercise “the degree of care that a person of ordinary prudence would exercise in dealing with the property of another person.” As well, it states that administrators should invest the pension funds assets “in a way that a reasonable and prudent person would apply to the investment portfolio of a pension fund.”

For its part, the *PBSR* require pension plan assets to be kept separate and apart from the employer’s own assets. The Regulations also set out investment and lending limits for pension funds, including:

- No more than 10 per cent of any pension fund may be invested in any one corporation or two or more affiliated corporations;
- A pension fund may not directly or indirectly acquire more than 30 per cent of the voting shares of a corporation; and
- Various restrictions on direct and indirect investments by pension funds in real estate and resource properties must be followed.

In addition, the *PBSR* require plan administrators to establish a written Statement of Investment Policies and Procedures and to outline the elements that it must include. Copies of this Statement are to be made available to plan members, retirees and other beneficiaries by plan administrators.