PBSA Annual Report

1996

Report on the Administration of the
Pension Benefits Standards Act, 1985
for the year ended March 31, 1996

The Honourable Paul Martin, P.C., M.P.
Minister of Finance
Ottawa, Canada
K1A 0A6

Dear Minister:

Pursuant to section 40 of the *Pension Benefits Standards Act, 1985*, I am pleased to submit to you the PBSA Annual Report which covers the period from April 1, 1995 to March 31, 1996.

Section 40 of the Act specifies that the report shall be laid before Parliament by the Minister within 15 days after the Minister receives it or, if Parliament is not then sitting, within 15 days thereafter that Parliament is sitting.

Yours very truly,

John R.V. Palmer
Superintendent

Ottawa, November 1996

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Report on the Administration
of the Pension Benefits Standards Act, 1985
for the Year Ended March 31, 1996

Introduction

This report is made pursuant to section 40 of the *Pension Benefits Standards Act, 1985* (the PBSA) which requires that, " The Superintendent shall, as soon as possible after the end of each fiscal year, submit to the Minister a report on

(a) the operation of this Act during that year,

(b) the extent to which inflation adjustments or other adjustments to pension benefits have been provided during that year, either voluntarily by employers or pursuant to collective agreements, as shown in information filed pursuant to section 12,

(c) the source of the funds used to make any adjustments referred to in paragraph (b), and

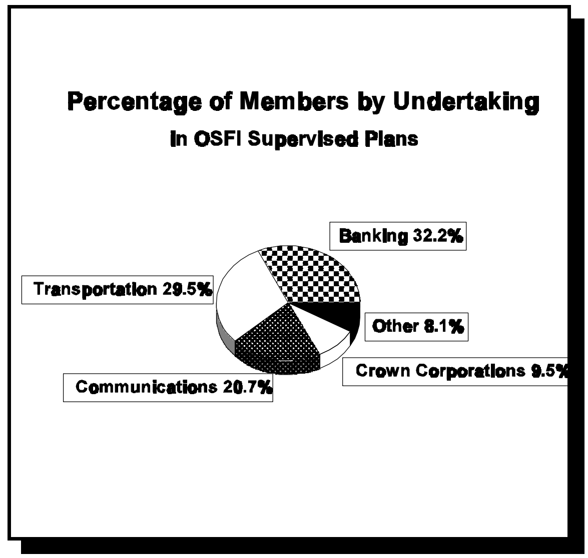
(d) the application of gains, if any, from pension funds".

Employer-sponsored pension plans, together with the Old Age Security, Canada/Quebec Pension Plans, Registered Retirement Savings Plans, and the *Income Tax Act* are the chief elements of the Canadian retirement system. Employer-sponsored pension plans are subject to rules that establish limits within which tax deductions are allowed for both employee and employer pension plan contributions. They are also subject to pension standards legislation designed to ensure minimum levels of protection for members and spouses and financial security of pension benefits.

The PBSA governs private pension plans established in respect of employees engaged in work that is subject to federal jurisdiction, such as banking, interprovincial transportation or telecommunications. All other private pension plans are governed by the laws of the province or provinces in which their members are employed.

The Office of the Superintendent of Financial Institutions (OSFI) regulates some 1,100 of Canada's 16,000 pension plans, covering more than half a million members.

The majority of members of PBSA plans, over 60 per cent, work in either banking or transportation (air, rail, road and water).



The PBSA came into force on January 1, 1987, repealing the *Pension Benefits Standards Act* (former Act) enacted in 1967. The legislation establishes 16 standards for registration which include, funding and investments, vesting, locking-in and portability of benefits, eligibility for membership, death benefits, and members' rights to information.

OSFI's Pension Benefits Standards Division is responsible for the day-to-day administration of the PBSA.

Operation of the PBSA for Fiscal 1995-1996

Pension plans filed under the PBSA

As at March 31, 1996, there were 1,108 active pension plans filed with OSFI. Five hundred and one thousand, two hundred and twenty-two (501,222) active employees participated in these plans. During the 1995-96 fiscal year, 67 new plans were filed for registration, and 71 previously filed plans were either terminated, delegated for provincial supervision, or consolidated with other plans. Consequently, the number of plans filed with OSFI decreased slightly, by 4, during the year. Table 1 reconciles the number of pension plans in force as at March 31, 1995 with the corresponding figures as at
March 31, 1996.

TABLE 1
Plans Filed*, Terminated, or Consolidated During the Year Ended March 31, 1996
(prior year's data in parenthesis)

	# Plans	**# Membership*****
Filed for registration during the year	67 (66)	4, 133 (5, 432)
Consolidated with other plans subject to the PBSA	22 (9)	n/a
Terminated **or delegated to a province during the year	49 (40)	1,191 (1,430)
In force at end of year	**1, 108 (1, 112)**	**501, 222 (507, 016)**

* Excludes 127 plans covering 282,762 members (the vast majority of whom are not subject to the PBSA) that were supervised by provinces on behalf of OSFI pursuant to reciprocal agreements - see *Agreements with provincial authorities* (page 11).

** A plan is recorded as being terminated in the year in which its assets are wound up and distributed to the members and other plan beneficiaries.

*** Membership is also adjusted to reflect latest data filed with the annual information return.

Distribution of Pension Plans and Membership by Type of Plan

While most pension plans (59 per cent) are of the defined contribution (money purchase) type, participants in defined benefit plans account for almost 89 per cent of the total membership of the 1,108 plans supervised by OSFI.

TABLE 2
Distribution of Plans and Membership by Plan Type
(as at March 31, 1996)

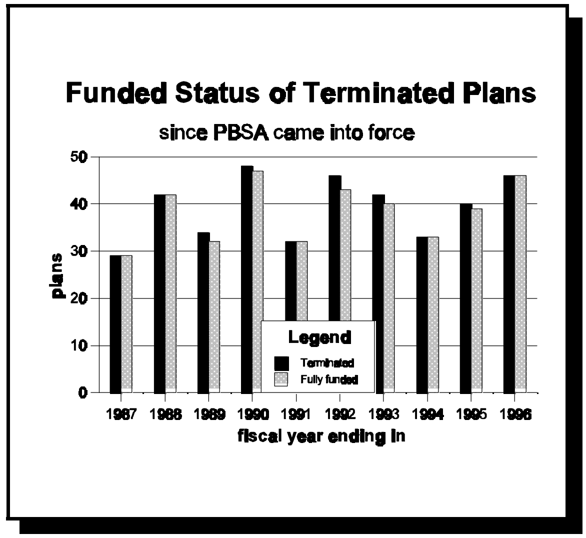
Plan Type	**#Plans**	**% of Total**	**# Members**	**% of Total**
Defined benefit				
< average best earnings	205		292, 214	
< f inal average earnings	100		74, 614	
< career average earnings	89		25, 745	
< flat benefit	25		14, 179	
< negotiated contribution	31		38, 474	
Total defined benefit	450	(41%)	445, 226	(89%)
Defined contribution (money purchase)	658	(59%)	55, 996	(11%)
Total	**1, 108**	**(100%)**	**501, 222**	**(100%)**

Plans terminations

In fiscal 1995-96, eleven hundred and three (1,103) employees had participated in the 46 pension plans that were terminated (excludes three that were delegated for provincial supervision). In each case, there was no loss of benefits to plan members. Reasons cited for termination included: no longer any active members; business sold; and, decision to switch to group registered retirement savings plans (RRSPs).

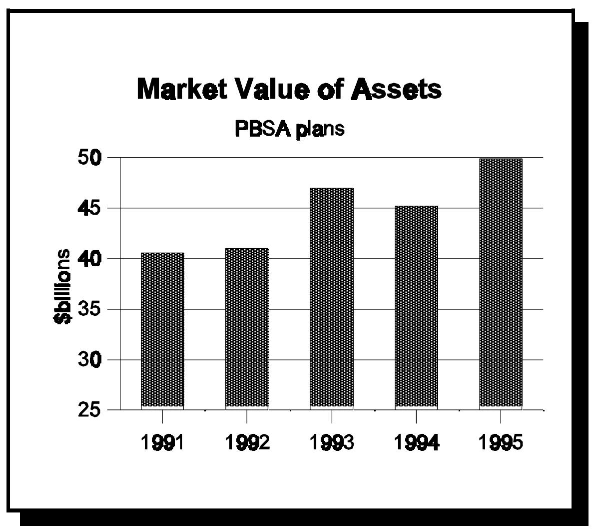
Funded Status of Terminated Plans Over the Years

Since the PBSA came into force in 1987, 392 plans terminated (i.e. assets were wound up and distributed). Of these, only nine terminated in a less than fully funded status. In most of the nine, the loss of benefits to members was minimal and the plans had a very small membership. In one plan only, members received less than 95 per cent of their pension benefit credit. In that case, the members received approximately 80 per cent.



Market Value of Assets Over the Years

The total market value of the assets of pension plans at the end of 1995 was approximately $49.9 billion, an increase of $4.7 billion or 10.5 per cent over 1994. Over the last five years, the assets of federally regulated plans increased by almost
23 per cent.



Reviewing Required Filings

Under the current regulatory regime, the analysts in the Pension Benefits Standards Division are required to review a variety of filings to assess compliance with the requirements of the PBSA. During the fiscal year, about 4,000 filings were received. Among these were new applications for registration, amendments to registered plans, annual information returns, audited or certified financial statements, actuarial reports, etc.

Monitoring Plans' Solvency

Early detection of potential solvency and funding problems are key success elements of the Division's monitoring program. This can only be accomplished through a thorough review of the financial and actuarial reports, and regular contact with the financial institutions holding the assets of the concerned pension plans. The analysis of the financial and actuarial reports allows analysts to detect potential non-compliance, such as late remittance of required contributions or improper administration of the plan. This work often results in plans being selected for a more comprehensive or more focused on-site examination.

Defined benefit plans must file an actuarial valuation report every three years unless the solvency ratio is less than one, in which case the filing is annually. An actuarial report must also be filed whenever a plan amendment affects the cost of benefits. The actuarial report describes the plan's financial situation and discloses the recommended contributions that are necessary to meet current service costs. The report also establishes the amounts of any solvency deficiency or unfunded liability together with schedules of special payments recommended for the amortization of these deficits. These schedules must comply with the requirements of the Regulations under the PBSA.

On-Site Examinations

During the fiscal year, 30 pension plans were examined at the site of plan administrators and their representatives. The examinations included a review of investment policies, records, accounts, controls and procedures used in connection with the administration of the plans.

The selection of plans for on-site examination is based primarily on risk to the beneficiaries. A risky plan would generally have one or more of the following characteristics: a low solvency ratio, late filing of reports, frequent complaints from members, major amendments to plan documents, etc. Each year, approximately 20 per cent of the plans to be examined are selected at random.

The examiners find that many plans are well run while others experience major problems which only an on-site examination can reveal. The examiners' findings over the years have included late remittance of contributions, improper calculation of contributions and benefits, potential funding problems, investment policies which are not being followed, improper administration with respect to eligibility for membership, and lack of information to members.

OSFI will examine approximately 40 plans during fiscal 1996-97.

Surplus refunds

The issue of entitlement to pension plan surplus arises in defined benefit pension plans. In these plans, beneficiaries are promised a fixed level of benefits defined through a pension formula. When there is a surplus of assets over liabilities in the fund established to pay the benefits, questions of entitlement arise.

Surplus refunds to employers are subject to the terms and conditions of the individual pension plan, and to compliance with regulations, irrespective of whether or not plan members are required to contribute to the plan. The documents which establish and describe a pension plan may contain provisions which address entitlement to surplus. However, most plans currently in existence do not contain provisions which allow for employer withdrawals of surplus (i.e. they are either silent or ambiguous in this regard), and most do not contain provisions which would allow the plan to be amended to grant such rights.

Section 9(5) of the PBSA allows surplus to be refunded to the sponsor of a going concern plan provided that the refund is permitted by regulations and provided that the Superintendent consents. Regulations give a definition of surplus, and establishes the amount of surplus that may be refunded and the conditions under which a refund may be made (which includes a 30 day notification period for plan members). In general, surplus must exceed the greater of 25% of the liabilities of the plan (calculated in prescribed manner) or 2 times the contribution of the employer to the normal cost of the plan, in order to qualify for a refund. Very few plans currently in surplus have levels of surplus above these thresholds.

During the period covered by this report, the Superintendent approved five requests for refunds of surplus to plan sponsors. The total amount refunded was $13.7 million, all in respect of plans that had terminated. Most of the surplus refund ($13.5 million) was in respect of one large pension plan. In the previous year, five requests were approved for a total of $3.8 million.

New Approach to Supervision

Current PBSA Supervisory Framework

In the years since the proclamation of the PBSA, some federally-regulated plans have experienced funding and solvency concerns and fortunately just a few were wound up without sufficient assets to pay the accrued benefits promised under the plan. OSFI's experience with these pension plans has clearly demonstrated the critical importance of good plan governance and solvency funding rules that promote the timely and cost-effective delivery of benefits and, at the same time promote the administration of the plan in the best interests of the plan members and beneficiaries. At present, the PBSA contains few corporate governance requirements.

During the same period some plans failed to meet one or more of the prescribed standards under the PBSA including, funding and solvency, investments, vesting, locking-in, members' rights to information, etc. Currently, where a pension plan fails to remedy a situation of non-compliance within a prescribed period, there is no enforcement method available to the Superintendent short of terminating the plan.

Also, OSFI is increasingly being asked to intervene in plan situations which are more appropriately the responsibility of plan administrators. The most common example of this involves disputes over terms and conditions of the plan not required by legislation that are provided in the various legal agreements and other documents that establish the plan, or by collective bargaining.

There is a need to review the PBSA at this time to clarify OSFI's role and responsibilities in regard to the supervision of pension plans and provide the Superintendent with the necessary authorities and powers to address the types of supervisory and prudential issues discussed above.

Proposed Changes to PBSA Supervisory Framework

In July 1996, the Federal Government released a White Paper on the enhancement of the supervision of private pension plans. The paper sets out the government's proposals to improve the supervisory regime for pension plans regulated under the PBSA and ensure that it remains up to date and effective in the evolving environment in which private pension plans operate. The paper was widely distributed and written submissions were invited to be made to OSFI by September 27, 1996.

The proposed amendments would extend OSFI's mandate contained in the OSFI Act, to clarify its supervisory role in regard to pension plans. In particular, it would acknowledge OSFI's role in monitoring the solvency of the pension plans that it regulates, in promoting policies that are designed to monitor and control risk, and in taking steps, or requiring that steps be taken, to deal promptly with problem plans.

Furthermore, the revised OSFI mandate would also help clarify that it is the administrator's responsibility to ensure continuing compliance with the PBSA and regulations, to oversee the operation of the plan and to deal with problems that may emerge.

The major policy initiatives undertaken in the paper are designed to:

- enhance plan governance measures, placing more emphasis on the importance of the duties and responsibilities of plan administrators and allowing employees more access to the administration of their plan;

- provide additional supervisory powers to the Superintendent, including the authority to issue formal directions to plans where, in the opinion of the Superintendent, imprudent or unsafe practices exist;

- require the administrator to provide more information to plan members on the financial condition of the plan;

- clarify certain requirements in respect of investment policies and propose alternatives for enhancing funding requirements; and

- make some technical changes to clarify and facilitate the administration of legislative requirements.

Pension Benefits Standards Division Communications

Newsletter - PBSA Update

The *PBSA Update* informs pension plan administrators and other players in the pension industry of changes to the PBSA legislation and regulations. The newsletter also serves to remind plan administrators and their representatives of particular PBSA standards and to inform them of changes in administrative policies and procedures. Most recent issues of *PBSA Update* were dated September 1995 and June 1996. Readers are encouraged to send their comments to OSFI on any matters covered in the newsletter or related to OSFI's supervision of pension plans.

Meetings with Plan Administrators

The management of the Pension Benefits Standards Division meets, usually annually, with the sponsors of about twenty large pension plans and their representatives to discuss their respective concerns. New initiatives being considered by OSFI are also discussed at these meetings. Agenda items have included the solvency and funding of plans, on-site plan examinations, the status of the proposed multi-lateral federal-provincial reciprocal agreement, and changes to regulations.

Audit and Actuarial Advisory Committees

The Pension Auditors' Advisory Committee is comprised of pension plan auditors and senior OSFI personnel. The committee meetings provide a forum for discussion of issues of mutual interest to auditors and OSFI. At the September 1995 meeting, items discussed included access to photocopying of pension plan documents and to the auditor's working papers by OSFI examiners, and the scope and role of auditors in monitoring contribution compliance of pension plans, valuation of special investments (e.g. mortgages), and allocation and reasonableness of union and trustee expenses.

The Pension Actuaries' Advisory Committee is made up of senior OSFI personnel and actuaries involved with pension plans subject to the PBSA. The committee met in Toronto in May 1995. Agenda items included discussion on a proposal for new funding regulations and a draft of the life income fund (LIF) regulation. The LIF regulation was approved in November 1995.

CAPSA Activities

The Canadian Association of Pension Supervisory Authorities (CAPSA) was established in 1974 as a federal-provincial forum in which to:

- work to ensure that pension plans that have members in more than one jurisdiction are regulated in a coordinated and orderly manner;
- to discuss and resolve supervisory problems and issues of an interjurisdictional nature relating to pension plans;
- to consider and, if appropriate, recommend measures for the benefit of pension plan members and sponsors; and
- to communicate with industry groups and professional associations on pension plan issues.

The following officials in charge of administering federal or provincial pension benefits standards legislation are represented in CAPSA:

Alberta	Superintendent of Pensions
British Columbia	Superintendent of Pensions
Government of Canada	Superintendent of Financial Institutions
Manitoba	Chairperson, Pension Commission of Manitoba
New Brunswick	Superintendent of Pensions
Newfoundland	Superintendent of Pensions
Nova Scotia	Superintendent of Pensions
Ontario	Chairperson, Pension Commission of Ontario
Quebec	Président, Régie des rentes du Québec
Saskatchewan	Superintendent of Pensions

Prince Edward Island, in which pension standards legislation has been passed but not proclaimed, will automatically be represented on CAPSA when the legislation comes into force. In the meantime, a representative has attended several CAPSA meetings. Representatives of Revenue Canada, Finance Canada and Statistics Canada have a standing invitation to attend CAPSA meetings.

During the year under review, meetings of CAPSA were held in September 1995 in Ottawa, and in March 1996 in Toronto. The proposed new multilateral reciprocal agreement (see item below) continues to be a main topic of discussion at CAPSA meetings, as does regulatory harmonization, flexible pension plans and simplified pension plans. Jurisdictional reports and papers are tabled and discussed at CAPSA meetings.

Agreements with Provincial Authorities

Prior to the extensive pension reform beginning in the mid-1980s, the relatively few differences among the various laws and regulations had enabled regulatory bodies to reach reciprocal agreements under which jurisdiction of registration is based on location and nature of employment. The regulatory body in the jurisdiction of registration applies the rules of other jurisdiction(s) where applicable. Increasing complexity of pension standards legislation has made this approach very difficult to implement.

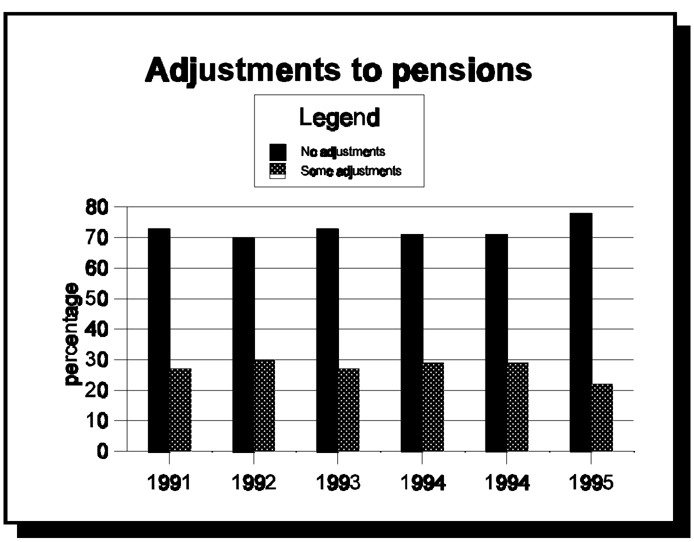
Recognizing that existing agreements merely allow a single regulator to apply a multiplicity of rules to a given plan, CAPSA has developed a new multi-lateral reciprocal agreement. The objective of the proposed agreement is to further reduce the administrative and compliance burdens facing the administrators of pension plans subject to more than one jurisdiction. While its adoption would leave unchanged the number of plans registered with the various jurisdictions, it would result in plans being governed in all matters by the pension legislation of the jurisdiction in which there is plurality of members. In other words, the supervising jurisdiction would no longer be required to ensure compliance with the standards of other jurisdictions. Some jurisdictions already have the powers to enter into the agreement while others, including the federal government, will have to amend legislation. So far, however, no government has signed the agreement.

Report on Provision of Inflation Adjustments to Pensions and Application of Gains from Pension Funds

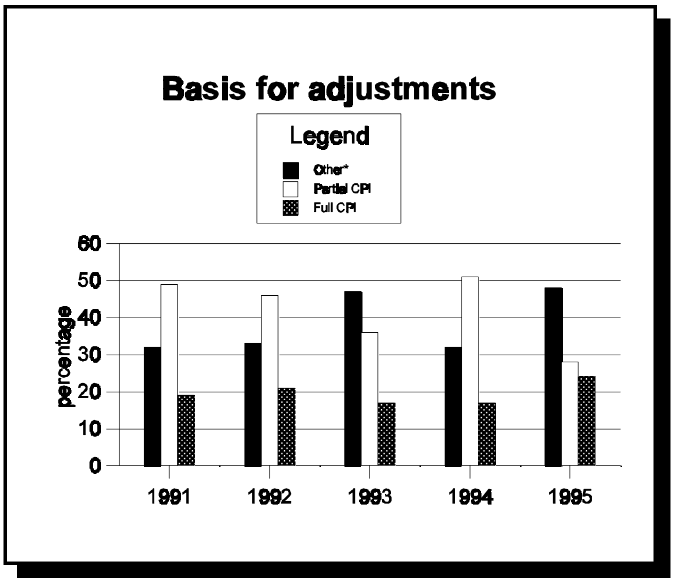
As required by the PBSA, plan sponsors report annually the extent to which they have adjusted pensions in order to provide inflation protection and the source of funds for these adjustments.

The practice of adjusting pension benefits in payment is normally observed only in respect of pensions arising out of defined benefit plans. Less than half of the plans subject to federal jurisdiction are of this type.

The following charts summarize the information on this subject as reported by pension plan sponsors for the calendar years 1991 through 1995, based on information filed at the time of report preparation.

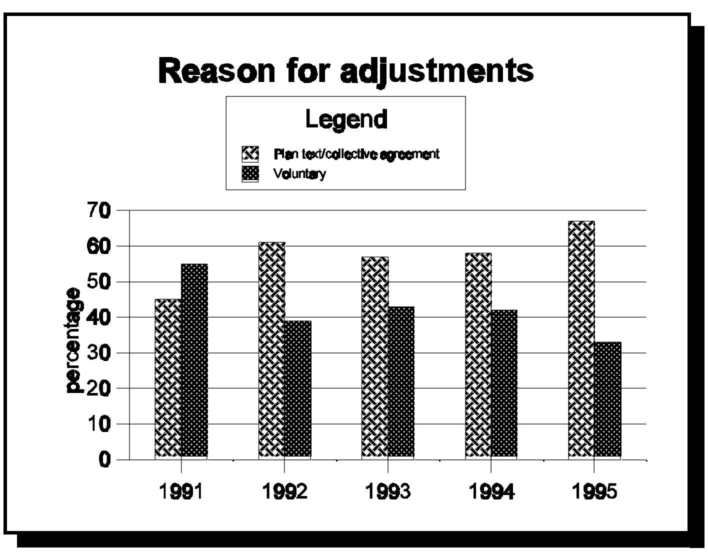


Of the defined benefit pension plans that had filed annual information returns in respect of the 1995 plan year end, 22 per cent reported that they had made some adjustments to pensions. This is down from 29 per cent in 1994.

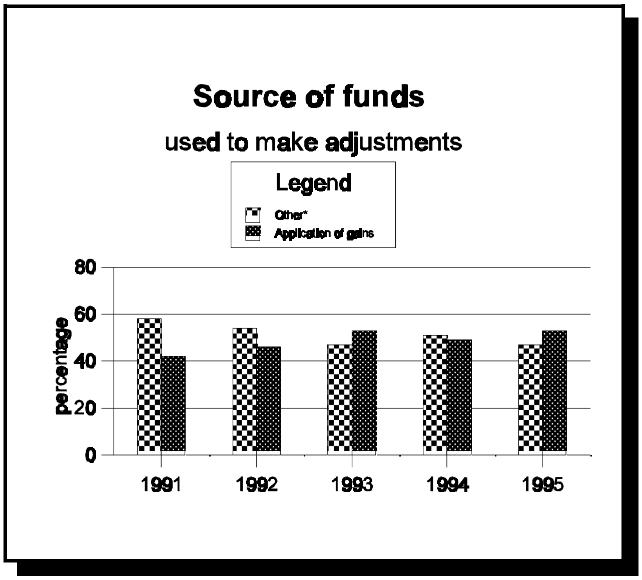


In 28 per cent of plans that made adjustments to pensions in 1995, benefits were partially indexed to the Consumer Price Index (CPI). Twenty four per cent (24 per cent) based on increases in the full CPI.

* excess interest formula, flat benefit and various formulae

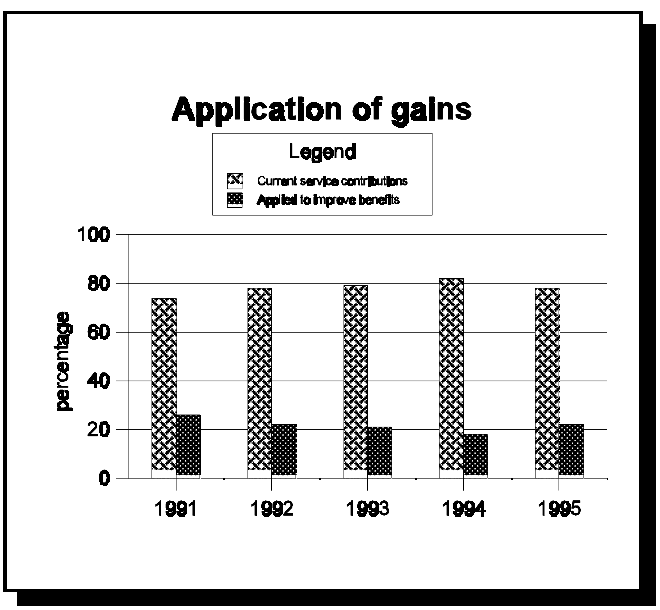


For the past four years, the majority of adjustments have been contractual as opposed to voluntary.



Over the past four years, in about half the defined benefit plans that made adjustments to pensions, the source of funds was gains from pension funds.

* Other - e.g. creation of unfunded liability, paid by employer



Data provided in the annual information returns indicates a relativelystable incidence of gains from pension funds being applied towards current service contributions.

Revenue and Expenditure for the Year Ended March 31, 1996

Pension plans are required to submit a fee with an application for registration under the PBSA and with the filing of the annual information return. Total fees received during the fiscal year ending March 31, 1996 amounted to $2,774,000 compared to $2,911,000 the previous year.

The total expense of administering the PBSA for fiscal 1995-96 was $2,772,000 compared to $2,792,000 for 1994-95.

Pursuant to regulations adopted by the Federal Government in 1991 to implement full cost recovery of the PBSA supervision program, commencing with the 1992-93 fiscal year any shortfall in revenue over expenditures is recovered by an increase in the fees in respect of annual information return filings. Similarly, any excess of fees received over administration costs are taken into consideration in setting the basic fee rate for subsequent years. This provision ensures that plan sponsors pay the full cost of administering the PBSA, but no more.

TABLE 3

Income, expenditure and basic fee rate for PBSA supervision since full recovery program was implemented

	1992-93	**1993-94**	**1994-95**	**1995-96**
Revenue	$2,899,000	$3,686,000	$2,911,000	$2,774,000
Expenditure	$2,704,000	$2,594,000	$2,792,000	$2,772,000
Basic fee rate	**$13.10**	**$10.25**	**$9.60**	**$10.50**

For plans with a year end between October 1, 1995 and September 30, 1996, the basic fee rate is $ 10.50 per plan member up to 1,000 members, and $ 5.25 per member in excess of 1,000. There is a minimum fee of $210 per plan, and a maximum of $ 105,000.
The basic fee rate for 1996-97 has now been established at $ 10.