Challenges for Jointly Sponsored Pension Plans

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Amidst the wave of pension reform in Ontario, one crest has peaked above the rest; jointly-sponsored pension plans ("JSPPs") are under close examination by the government and the public. While JSPPs have proven to be a successful model of pension governance, they present some unusual governance challenges for stakeholders and advisors.

In this paper, we explore the current JSPP framework before moving to the very recent initiatives of the Ontario Government. As announcements continue up to the date of this writing, we offer no predictions for the future of JSPPs but the most obvious: successful growth of JSPPs in Ontario will require cooperation and compromise from all stakeholders, including government, members and sponsors.

A. What's a JSPP?

A JSPP is a contributory, defined benefit pension plan in which all contributing stakeholders and plan members have decision making and funding responsibility.

> For the purposes of this Act, a pension plan is a jointly sponsored pension plan if it has the following characteristics:
>
> 1. It provides defined benefits.
>
> 2. The defined benefits are contributory benefits.
>
> 3. Members of the pension plan are required, by virtue of the documents that create and support the plan, to make contributions in respect of any going concern unfunded liability and solvency deficiency of the plan.
>
> 4. The plan satisfies such additional criteria as may be prescribed.[1]

[1] Ontario *Pension Benefits Act*, R.S.O. 1990, c.P.8, s. 1(2) (the "PBA").

The PBA general regulation[2] also makes the following special provisions with respect to JSPPs:

> 3.1(1) For the purposes of paragraph 4 of subsection 1 (2) of the Act, a pension plan must, by virtue of the documents that create and support the plan, satisfy the following additional criteria in order to be a jointly sponsored pension plan:
>
> 1. The total amount of contributions payable by members of the pension plan in respect of a year, excluding any additional voluntary contributions and voluntary contributions for past service as described in subsection 39 (5) of the Act, cannot exceed the total amount of contributions payable to the pension plan in respect of the year by the employer or by the person or entity required to make contributions on behalf of the employer, as the case may be.
>
> 2. The pension plan does not permit a reduction in the amount of or the commuted value of a pension benefit, a pension, a deferred pension or an ancillary benefit in the circumstances described in subsection 14 (2) or (3) of the Act, except in the circumstances of a wind up.
>
> 3. The employers or any persons or entities who make contributions on behalf of the employers or represent the employers and the members of the pension plan or any representatives of the members are jointly responsible for making all decisions about the terms and conditions of the pension plan and any amendments to the pension plan.
>
> 4. The employers or any persons or entities who make contributions on behalf of the employers or represent the employers and the members of the pension plan or any representatives of the members are jointly responsible for making all decisions regarding,
>
> i. the appointment of the administrator of the plan, or
>
> ii. the appointment or selection of persons as members of any body or entity referred to in clause 8 (1) (b), (c), (e), (f) or (h) of the Act that is the administrator of the plan.

[2] O.Reg. 909.

> 5. The level of a member's pension benefits, other than ancillary benefits, and the amount of a member's contributions are directly related to the member's pensionable earnings.

Of note, as of July 1, 2012, JSPPs may elect to exclude plan members from the grow-in provisions of the PBA.[3]

At present, JSPPs are found primarily in the public sector, and include the Ontario Teachers' Pension Plan ("OTPP"), the Healthcare of Ontario Pension Plan ("HOOPP"), the Ontario Municipal Employees Retirement System ("OMERS"), the Colleges of Applied Arts and Technology Pension Plan ("CAAT") and the OPSEU Pension Trust ("OPT").

A JSPP is similar to a multi-employer pension plan (a "MEPP"), which is a collectively bargained pension plan that covers the employees of more than one employer.[4] However, a MEPP must be governed by a board of trustees on which both employer and employees participate.[5]

B. JSPPs in the Wild

Unlike multi-employer pension plans ("MEPPs"), JSPPs have a certain amount of leeway in their governance structure, as long as there is some variety of joint decision making. Most JSPPs, like MEPPs, are governed by boards of trustees or directors, but sponsor participation varies. Generally, however, plan sponsors (both government, employers or unions) retain control of

[3] PBA, s. 74.1

[4] PBA s. 1(3).

[5] PBA s. 8(e). If a MEPP is established by statute, other arrangements can be made.

benefit design and funding, while the boards of trustees or directors administer the plan. This structure looks familiar to those used to single employer pension plans, but there are a few twists.

a) Ontario Teachers' Pension Plan

The OTPP is governed by the *Teachers' Pension Act*,[6] which establishes the Ontario Teachers' Pension Plan Board as a corporation without share capital. The TPA provides that the Minister of Education and the executive of the Ontario Teachers' Federation (the "OTF"), which is an association of the major teachers' unions in Ontario, may enter into an agreement to provide for, among other things, the "joint management" of the pension plan by the Minister and the OTF and the "sharing of entitlement to gains or surplus under the plan and of liability for deficiencies in the pension fund by the Minister, the employers who contribute under the plan and the active plan members."[7]

Pursuant to the TPA, the Minister and the OTF, the sponsors of the OTPP, entered into an agreement in 1992. Under that agreement, the partners agreed to be jointly responsible for plan gains and losses.[8]

b) The Healthcare of Ontario Pension Plan

HOOPP is governed by a Board of Trustees, eight of which are appointed by the Ontario Hospital Association, and eight of which are appointed by the four participating unions. HOOPP

[6] R.S.O. 1990, c.T.1 (the "TPA").

[7] TPA s. 10.

[8] http://www.otpp.com/wps/wcm/connect/otpp_en/Home/Corporate+Info/Plan+Governance/Plan+Sponsors+Role/

was established under an Agreement and Declaration of Trust for the benefit of eligible employees of participating employers.

c) Colleges of Applied Arts & Technology Pension Plan

CAAT has three plan sponsors: Colleges Ontario, acting on behalf of the Boards of Governors of the Colleges, the Ontario College Administrative Staff Association and the Ontario Public Service Employees Union. There is a Sponsors' Committee, responsible for benefits and funding, and a Board of Trustees, responsible for the administration of the pension plan. The roles of each body are outlined in a Sponsorship and Trust Agreement.

d) OPSEU Pension Trust

OPT is also governed by a Board of Trustees, half of which is appointed by the Government of Ontario, and the other half by OPSEU. The sponsors retain decision making responsibility for plan design, benefits and funding, while the Board of Trustees administers the plan.

e) OMERS

OMERS, under the *OMERS Act, 2006*,[9] has a unique structure. The *OMERS Act, 2006*, established two separate corporate bodies: the Administration Corporation (the "OAC") and the Sponsors Corporation (the "SC"). The SC is responsible for plan design and funding, including the setting of contribution rates. The OAC is primarily responsible for the administration and investment of the plan as well as providing technical support to the SC. Members of the OAC

[9] S.O. 2006, c.2.

and the SC are appointed as set out in the By-Laws of the SC, which provide for appointments by participating employers, employer groups, unions and representatives of retired members.

After this structure was established in 2006, questions arose regarding the implementation of the varying spheres of responsibilities, especially with respect to funding. A case was brought in the Ontario Superior Court by both entities to have the court's approval given to a joint framework; that having been achieved, the two corporations continue to govern the plan.[10] A review of the governance structure is statutorily mandated for 2012.[11]

[10] *OMERS Sponsors Corporation v. OMERS Administration Corporation*, 2008 CanLII 3970 (ON SC).

[11] *Ontario Municipal Employees Retirement System Review Act, 2006*, SO 2006, c 9, Sch K.

The size of the plans and the contribution rates are as follows:

Plan	Assets ($ Billions)	Active Members	Employee Contribution Rate	Employer Contribution Rate
OPT	13.3	47,000	9.4/11[12]	9.4/11
OTPP	107.5	175,000	10.8/12.4[13]	10.8/12.4
HOOPP	35.7	170,000	6.9/9.2[14]	8.7/11.6
CAAT	5.5	19,000	11.1/12.9[15]	11.1/12.9
OMERS	55.1	257,000	NRA 65: 8.3/12.8 NRA 60: 9.4/13.9[16]	8.3/12.8 9.4/13.9

f) Funding Features

JSPPs are unique in their funding structures. As we saw above, JSPPs are funded through contributions from employers and employees, and both parties are responsible for funding any deficiencies. Contributions may be increased, or benefits reduced, to meet the funding challenge. This is the "trade-off" for joint governance; employees and sponsors bear the funding

[12] Rates below and above YMPE: see http://www.optrust.com/Employers/EmployersUpdates/empu42_December2011.asp#1

[13] Rates are below and above YMPE: see http://www.otpp.com/wps/wcm/connect/otpp_en/home/member+info/contributions/contribution+rates+-+2009/contribution+rates+-+2012

[14] Rates are below and above YMPE, and Employers contribute 126% of what members contribute: see http://hoopp.com/Employers/Newsletter-primer/2011-issue-2/Contribution-rates-remain-unchanged-until-the-end-of-2013/

[15] Rates are below and above YMPE: see http://www.caatpension.on.ca/en/members/member-newsletters/contribution-changes-2012

[16] OMERS Rates are NRA 65 and NRA 60, below and above YMPE – see http://www.omers.com/pension/members_news_article.aspx?newsid=4283

risk. However, JSPPs are exempt from solvency funding requirements for all valuation dates after December 31, 2010.[17]

C. Implications of Governance and Funding Structures

The participation of all stakeholders in a JSPP is a necessary condition for its success. As the discussion above demonstrates, both employers/government and unions/members must have active participation in the governance of these plans. Difficulties can arise when the representatives meet at the table as trustees or directors; appointed as representatives of interest groups, the interest they must now represent is that of the pension plan they govern. In some circumstances, an increase in contribution rates or a decrease in benefits may not be in the best interests of one stakeholder group, but is in the best interest of the pension plan as a whole. All representatives must struggle with these choices; in our experience, this is something boards of trustees and directors take extremely seriously, and wrestle with at all times. The changes on the horizon will not assist in making these choices.

D. Changes are Ahead

While most JSPPs are large and successful they are coming under increased scrutiny by the Ontario government, which, along with the plan members, shares the funding risk for most of these plans. In the case of OMERS, participating employers in the municipal sector share the risk. There have been three recent developments of significance, as discussed below.

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[17] O.Reg. 177/11.

a) The Drummond Report

On February 14, 2012, Chair Don Drummond released the Report of the Commission on the Reform of Ontario Public Services (the "Drummond Report"). In that report, in the section entitled, ominously, "Liability Management", Drummond discusses Ontario's broader public sector pension plans, which are the majority of Ontario's JSPPs.

Drummond's major concern is with the funding of the JSPPs, and the province's responsibility for funding.[18] It is important to note that Drummond's concern is not primarily with funding measures as typically understood in the pension industry, but rather how funding liabilities appear on provincial financial statements, the accounting valuation, which is based on the present value of benefits earned by plan members (not contributions).

He notes that there is "considerable confusion" regarding who has the "ultimate financial responsibility" for funding the deficits, if any, in these plans.[19] While he offers no suggestions to alleviate the confusion, his suggested approach is designed to reduce the government's prospective liability.

Accordingly, in order to address these funding deficits, Drummond did not recommend contribution increases, but rather recommended:

> The government's objective, when faced with pension funding deficits, should be to reduce the prospective benefits rather than increase the contribution rate beyond current levels. This would help to close the funding gap and reduce the accrual of pension

[18] The Province has no responsibility for the funding of OMERS.

[19] Drummond Report, section 19-5.

> benefits on a prospective basis, mitigating the impact on the fiscal plan. The government may need to consider legislative options, should negotiations with plan sponsors be unsuccessful. [20]

As noted above, contribution control will not sufficiently address the government's accounting issues, as it is the present value of benefits that are reflected on the balance sheet. Accordingly, Drummond suggests that benefit adjustments will also need to be made, if employees are not willing to increase their proportion of the contributions. An increase in employee-side contributions would also require amendments to the PBA and the ITA. Accordingly, Drummond recommends that government should undertake negotiations to reduce benefits on a prospective basis, such as changes to indexation or early retirement provisions.[21]

b) Ontario's 2012 Budget

In the 2012 budget, the Ontario government announced its intention to follow up on some of the recommendations in the Drummond report, including the recommendation that all JSPPs move to 50-50 funding between employers and employees.

[20] Drummond Report, section 19-8.

[21] Drummond Report, section 19-9.

c) Consultations

On April 25, 2012, the government announced that it will begin consultations with stakeholders in the JSPP sector to develop legislative reforms. Notably, the government has clearly signaled that any such reforms will have the following characteristics:

- in case of a deficit, plans would be required to reduce future benefits or ancillary benefits before further increasing employer contributions;
- in exceptional circumstances, a limit would be set on the amount or value of benefit reductions before additional contribution increases could be considered;
- any benefit reductions would involve future benefits only, not those that have already been accrued. Current retirees would not be affected;
- where employee contributions are currently less than employer contributions, increased employee contributions would also be available as a tool to reduce pension deficits;
- where plan sponsors cannot agree on benefit reductions through negotiation, a new third-party dispute resolution process would be invoked; and
- the framework would be reviewed after the budget is balanced.[22]

E. Implications of Recent Developments

The immediate concern and challenge ahead is stated in the Drummond recommendation as follows: JSPPs need to consider benefit changes before contribution raises for employers, or the government will consider it for them. The tensions that this type of statement can create in the

[22] Ontario Minister of Finance, News Release, "McGuinty Government Making Public Sector Pensions More Sustainable, Affordable", April 25, 2012.

community are obvious. The success of JSPPs is predicated on economies of scale which are possible because all stakeholder groups can actively and concretely participate. Where one group takes an option off the table, be it a government which will not consider contribution increases, or a union that will not consider benefit reductions, the best interests of the plans can be lost. We anticipate that pension-related issues in the broader public sector, particularly with respect to JSPPs, will be a focus of legislative reform in the future.

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